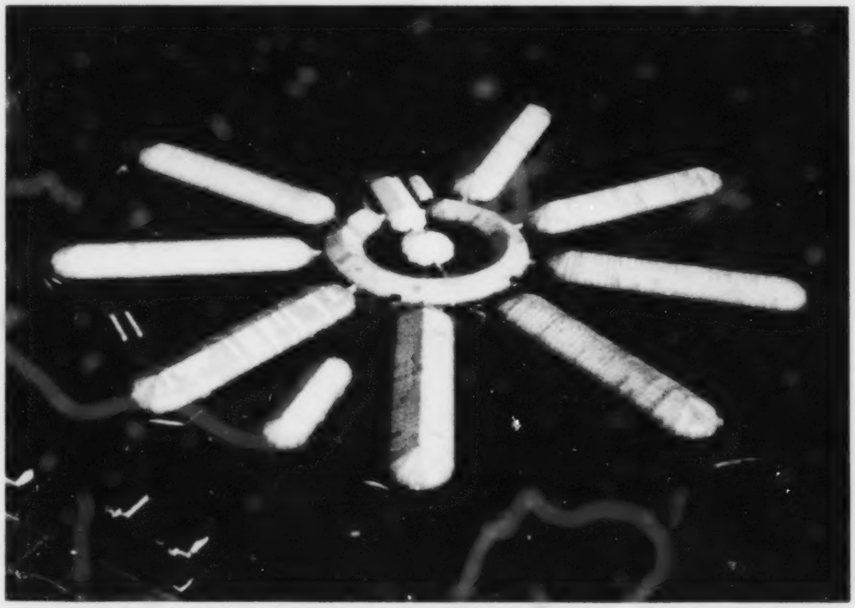
GOVERNMENT OF
NEWFOUNDLAND
AND LABRADOR

Royal Commission of Enquiry Into The Involvement of The Government of Newfoundland and Labrador and any of its Agencies or Corporations with Sprung Sales Limited, Sprung Environmental Space Enclosures Limited or Newfoundland Enviroponics Limited



REPORT

Findings And Recommendations

Submitted by:
The Hon. Mr. Justice S. O'Regan
Commissioner

92-06563/

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Newfoundland and Labrador

The Honourable
Mr. Justice S. O'Regan
Commissioner

F. Bruce Winsor, Q.C.
Commission Counsel

Weldon H. Orser
Executive Secretary

Royal Commission Of Inquiry Into The Involvement of
The Government of Newfoundland and Labrador and any of its
Agencies or Corporations with Sprung Sales Limited,
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TO HIS HONOUR
THE LIEUTENANT GOVERNOR IN COUNCIL:

May it please your honour,

I, Seamus Bernard O'Regan, appointed a Commissioner under the Public Inquiries Act Revised Statutes of Newfoundland, 1970, Chapter 314 by letters patent issued to an Order in Council dated the first day of July 1990 to enquire and report as therein directed and by an Extension thereto granted by Order in Council dated the 13 day of November 1991 to enquire and report as therein directed.

I beg to submit to your Honour my report all of which I respectfully submit for your Honours consideration.

The Honourable
Mr. Justice S. O'Regan
Commissioner

ROYAL COMMISSION STAFF

COMMISSIONER

The Honourable Mr. Justice
Seamus B. O'Regan

COUNSEL

Mr. F. Bruce Winsor, Q.C.

FORENSIC ACCOUNTANT

Mr. Bernard E. Beckett, F.C.A.

EXECUTIVE SECRETARY/INVESTIGATOR

Mr. Weldon H. Orser

SUPPORT STAFF

Ms. Colleen Power

Ms. Carolyn Abbott

Ms. Dawn English
(26 September 1990 - 15 June 1991)

ACKNOWLEDGEMENTS

As the Commissioner of this Royal Commission, I would like to acknowledge the efforts of Commission staff, without whom this report would not have been possible.

I am advised the majority of persons interviewed did so on a voluntary basis without the necessity of a subpoena and I thank them for their co-operation.

I would like also to acknowledge the co-operation of the various private companies involved in the construction of the facility who kindly provided Commission staff with access to records and personnel which has proven extremely helpful.

Finally, I wish to acknowledge the co-operation of the Government of Newfoundland and Labrador which, through the various departments directly involved in the work of the Commission, had to respond to numerous requests for information as well as access to files and personnel.

The Honourable
Mr. Justice S. O'Regan
Commissioner

THE COMMISSION

ELIZABETH THE SECOND, by the Grace
of God of the United Kingdom, Canada
and Her Other Realms and Territories
QUEEN, Head of the Commonwealth,
Defender of the Faith.

LIEUTENANT-GOVERNOR:

Minister of Justice

COMMISSION

TO: The Honourable Mr. Justice Seamus O'Regan

WHEREAS Newfoundland Enviroponics Limited was established in 1987 pursuant to arrangements between Sprung Sales Limited, Sprung Environmental Space Enclosures Limited, Newfoundland Industrial Development Corporation and Her Majesty the Queen in Right of Newfoundland;

AND WHEREAS the purpose of the joint venture so constituted was to construct a facility in Newfoundland for the cultivation, production, processing and marketing of horticultural products and related research and development;

AND WHEREAS the development has resulted in direct financial losses to the Province.

AND WHEREAS the Auditor General of Newfoundland on January 17, 1990 has advised the Lieutenant-Governor in Council with respect to apparent deficiencies in the manner and extent of governmental involvement in the project;

NOW KNOW YE that under and by virtue of The Public Enquiries Act, Chapter 314 of the Revised Statutes of Newfoundland, 1970, We, by and with the advice of Our Executive Council of Our Province of Newfoundland, reposing great trust and confidence in your knowledge, integrity and ability, have constituted and appointed and do by these Our Presents constitute and appoint you the said

The Honourable Mr. Justice Seamus O'Regan

to be a Commissioner to hold an enquiry into the matters foregoing, without limiting the generality of the foregoing, and any other matters associated therewith, that is to say:

1. To enquire into the involvement of the Government of Newfoundland and Labrador and any of its agencies or corporations with Sprung Sales Limited, Sprung Environmental Space Enclosures Limited, or Newfoundland Enviroponics Limited and in particular to determine
   - (a) whether the expenditure of and accounting for government financial and other assistance was in all respects proper, and properly managed and accounted for;
   - (b) whether any Acts and Regulations of the Province of Newfoundland were not complied with;
   - (c) whether or not there were breaches of any of the arrangements or agreements between the Government of Newfoundland and Labrador and any of the companies;
   - (d) whether there was any other aspect of governmental involvement in the matter that had a significant adverse impact on the interests of the Province and should be brought to the attention of the Lieutenant-Governor in Council;

2. AND FURTHER, We require you, the Commissioner, to bring forward conclusions and recommendations with respect to measures which may be taken by the Government of Newfoundland and Labrador to prevent any future developments being undertaken without appropriate safeguards.

AND WE DO, by these Presents, confer upon you, the said Commissioner, the power of summoning before you any witness or witnesses and of requiring all such witnesses to give evidence orally or in writing upon oath or upon solemn affirmation, and to produce such documents and things as you, the said Commissioner, may deem requisite to the full investigation of the matters you are appointed to enquire into;

AND WE DO, by these Presents, authorize you, the said Commissioner, to have access to all appropriate documents in the possession of the Government of Newfoundland and Labrador;

AND WE DO, by these Presents, authorize you, the said Commissioner, to adopt such procedures and methods as you, the said Commissioner, may from time to time deem expedient for the proper conduct of this Enquiry and to sit at such times and places as you, the said Commissioner, may from time to time decide, subject to the proviso that all such hearings must be held in a public place;

AND FURTHER, We require you to report your findings with as little delay as possible and in any event within six months from the date hereof.

IN TESTIMONY WHEREOF We have caused these Our Letters to be made Patent and the Great Seal of Newfoundland to be hereunto affixed.

WITNESS: Our trusty and well-beloved the Honourable James A. McGrath, a Member of Our Privy Council of Canada, Lieutenant-Governor in and for Our Province of Newfoundland.

AT OUR GOVERNMENT HOUSE in Our City of St. John's this 1st day of July, in the year of Our Lord one thousand nine hundred and ninety and in the thirty-ninth year of Our Reign.

BY COMMAND,

REGISTRAR GENERAL

THE NEWFOUNDLAND GAZETTE
November 22, 1991

NEWFOUNDLAND REGULATION 222/91

Proclamation re: Extension of Sprung Public Enquiry
under
The Public Enquiries Act
(O.C. 784-91)

(Filed November 19, 1991)

ELIZABETH THE SECOND, by the Grace of God of the United Kingdom, Canada and Her Other Realms and Territories, QUEEN, Head of the Commonwealth, Defender of the Faith.

(L.S.)
Frederick W. Russell
Lieutenant-Governor

Aubrey T. Gover
Minister of Justice

COMMISSION

TO: HONOURABLE MR. JUSTICE SEAMUS O'REGAN

WHEREAS that under and by virtue of *The Public Enquiries Act*, Chapter 314 of The Revised Statutes of Newfoundland, 1970, WE, by and with the advice of the Executive Council of Our Province of Newfoundland, reposing great trust and confidence in your knowledge, integrity and ability, have constituted and appointed, on July 1, 1990, the Honourable Mr. Justice Seamus O'Regan to be a Commissioner to hold an enquiry into the involvement of the Government of Newfoundland and Labrador and any of its agencies or corporations with Sprung Sales Limited, Sprung Environmental Space Enclosures Limited, or Newfoundland Environponics Limited and other matters associated therewith;

AND WHEREAS the findings of the said Commission were to be reported with as little delay as possible and in any event within six months from the date thereof;

AND WHEREAS We have deemed it necessary and expedient to extend the time for the filing of a final report of the Enquiry;

WE DO, by these Presents, authorize an extension of the time for the filing of a final report of the Enquiry and require you, the said Commissioner, to report your findings by December 31, 1991.

IN TESTIMONY WHEREOF, We have caused these Our Letters to be made Patent and the Great Seal of Newfoundland to be hereunto affixed.

WITNESS: Our trusty and well-beloved the Honourable Frederick W. Russell, Lieutenant-Governor in and for Our Province of Newfoundland.

AT OUR GOVERNMENT HOUSE in Our City of St. John's, this 13th day of November, in the year of Our Lord one thousand nine hundred and ninety-one and in the fortieth year of Our Reign.

BY COMMAND,

ERIC GULLAGE
Registrar General

FORWARD

In June of 1987, the Government of Newfoundland and Labrador through Newfoundland Industrial Development Corporation (NIDC) and two of Philip Sprungs companies entered into a joint venture through a company called Newfoundland Enviroponics Limited to construct a hydroponic greenhouse facility in Newfoundland for the cultivation, production, processing and marketing of horticultural products, initially cucumbers and tomatoes and for associated research and development.

On March 03, 1989, Newfoundland Enviroponics Limited was placed in Receivership resulting in direct financial losses to the Province.

On July 1st, 1990, the Lieutenant Governor in Council by Commission established this Royal Commission setting forth specific terms of reference as therein set forth by paragraph 1 and with instructions as noted by paragraph 2 therein to:

"bring forward conclusions and recommendations with respect to measures which may be taken by the Government of Newfoundland and Labrador to prevent any future developments being undertaken without appropriate safeguards."

To fulfil its mandate, this Royal Commission had to first determine the facts and circumstances surrounding the joint venture as well as undertaking a review of all sources of revenue as well as all sources of expenditures.

In achieving the accounting review, it was necessary to reconstruct the entire financial process which was painstakingly undertaken by Mr. Bernie Beckett, F.C.A., a Forensic Accountant and Managing Partner with the firm Peat Marwick Thorne.

To formulate the reports findings, it was necessary for Commission Counsel, Mr. F. Bruce Winsor, Q.C. to interview numerous witnesses and review some tens of thousands of documents. In addition some sixteen volumes of references referred to as Commission Documents in this report were prepared by Mr. Winsor and Mr. Beckett, with the assistance of Mr. Weldon Orser from the hundreds of volumes of documents which came into possession of Commission Staff.

In September and early October 1991, Notice of Applications for Standing was published in the various print media throughout the province. On October 18, 1991 at the hearing of Applications for Standing there appeared counsel on behalf of Government, the Department of the Auditor General and the Sprung noted Companies. The hearing was adjourned to November 14, 1991 and subsequently adjourned sine die to permit the compiling of a final investigative report to the Minister of Justice with recommendations as to the courses of action that may be taken by the Commission.

I do also mention that counsel for the Commission after the Hearing for Applications for Standing was notified by one Dr. W.S.W. Nowak of Memorial University of his intention to seek standing before the Commission of Enquiry. The basis for his application is outlined in his written report dealing with "the Prospects of Hydroponics and the Sprung complex in Mount Pearl, Newfoundland" and is noted in Commission Document CD 006 at page 147.

My review of all appropriate documentation together with the submissions and findings of Counsel and the Commission's Forensic Accountant as outlined in the report has enabled me to fully endorse the report's findings.

On the basis of further submissions of Commission Counsel and the Commission's Forensic Accountant, together with my review of the report's contents and appropriate documentation I am prepared to make recommendations, without the benefit of public hearings, pursuant to paragraph 2 of the Commission (Terms of Reference) and have done so.

I would only add it is truly hoped Governments realize the error of their ways in becoming involved financially in ventures of similar circumstance that one can classify only as high risk and to the peoples' detriment.

PART II

OVERVIEW

Late in 1986, Charmar Holdings Limited, a Newfoundland Company approached Government seeking financial assistance to construct and operate a system for growing fruits and vegetables in the Province similar to one then in existence in Calgary, Alberta and operated by Philip Sprung. The Company indicated that it had obtained the exclusive territorial rights to purchase and use the "Sprung Environmental Space Enclosure Food Production Facilities" in Newfoundland and Labrador. The growing system had been developed by the Sprung Group of Companies of Calgary, whose principal was Philip Sprung.

Sprung maintained The Sprung Group had invested $35,000,000 in extensive research and development activities over a 10 year period to perfect the technology. It was also claimed that the fabric that covered the Facility provided greater light to plants than traditional greenhouses and a computerized environmental control system accurately monitored and controlled different ingredients essential to plant growth. Through the combination of the Sprung Enclosure and the Girocrop Nutrient Film Technique (a system of crop production without soil or any other rooting medium, developed by Girocrop Limited, a British Firm), it was reported the Facility could produce 6.7 million pounds of saleable product (tomatoes and cucumbers) in its first year of operation, with annual market production increasing to 9.0 million pounds by the end of the fifth year.

THE CHARMAR PROPOSAL

Government Cash Grant	$ 2,500,000
Land Grant (NLHC Book Value)	70,000
Infrastructure Improvements	1,000,000
Provincial Sales Tax Exemption	900,000
Total Direct Support (Non Repayable)	**$ 4,470,000**
Provincial Loan Guarantee	10,000,000
Total Government Support	**$ 14,470,000**
Charmars Equity Investment	$ 1,000,000
	$ 15,470,000

The Capital cost of establishing a Calgary type Facility in Newfoundland would be $15,470,000 excluding Federal Sales Tax with a working capital loan guarantee from Government of up to $2,000,000 for three years.

GOVERNMENT ASSESSMENT

The Premier and officials of Government viewed the Calgary Facility in late 1986.

A Government assessment team comprising of Senior Civil Servants visited Calgary in early 1987 to view and assess the Calgary Facility.

Accompanying the assessment team to Calgary was the Supervisor of Crop Production for the Department of Rural, Agricultural and Northern Development (R.A.N.D.). He was very sceptical about the process and maintained that he received no evidence from his visit to the Facility and from the actual production figures presented, that the proposed yields provided by the Sprung Group could be obtained under Newfoundland climatic conditions. He suggested that no greenhouse Facility in the world was attaining such production yields. He also noted that light levels in Newfoundland during the period October to March are such that production levels would be drastically reduced and the economics of greenhouse vegetable production would be questionable.

Sprung subsequently offered to provide an artificial lighting system at the Facility with all operating and capital expenditures to be his responsibility. Sprung proposed to recover these costs from profits in excess of those projected in the Charmar proposal which Sprung asserted would occur because of higher production levels resulting from the artificial lighting.

Subsequently, Charmar Holdings Limited's involvement in the proposed venture ceased and Government dealt directly with the Sprung Group of Companies.

In April 1987, the assessment team again went to Calgary in an attempt to assess the reasonableness of the proposed purchase price and to meet with Sprung's bank to determine whether Sprung had the financial ability to meet the obligations being contemplated in the proposed venture. With respect to valuation, it was difficult to determine what the value of such a Facility was, given its unique nature. A review of Sprung's internal accounting records was undertaken and it was concluded that the cost of a new Facility could be placed in the range of $13,500,000 taking into account Sprung's actual outlay for components of the Facility and Sprung's selling prices for similar-sized structures to clients such as the Canadian Government and the United States military.

Subsequently, ongoing negotiations concluded with Sprung as an equity partner, the used Calgary Facility would be moved to the Province with warranties as if the Facility were new, and Sprung would not now finance the capital cost of the lighting system. The lighting system would be financed by way of a lease, which Sprung was to arrange, the payments on which would be the sole responsibility of a joint venture company without any Government guarantees.

AGREEMENT-IN-PRINCIPLE (HEADS OF AGREEMENT)

The basis of a financing package to establish a hydroponics Facility in the Province was tentatively agreed upon and on May 8, 1987 Cabinet authorized the

Honourable The Premier and other Honourable Ministers he deemed appropriate, to execute a "Heads of Agreement" based on the following financial package:

Government Equity	$ 3,500,000
Sprung Equity	3,500,000
Government Guaranteed Loan	7,000,000
Sprung Guaranteed Loan	500,000
	$14,500,000

The $14,500,000 was to cover, the purchase price of the Facility being $13,500,000, and the cost of land and associated infrastructure improvements being $1,000,000. Sprung was also to ensure leasing arrangements would be available to the joint venture Company for the acquisition and installation of growing lights at an estimated cost of $3,000,000.

Government also agreed to provide the joint venture Company with a Retail Sales Tax exemption associated with construction and equipping the Facility, estimated at $900,000.

THE FINALIZED FINANCIAL PACKAGE

1. **Government Contribution**

- Equity Infusion	$ 3,500,000
- Retail Sales Tax Remission relating to Facility construction & equipping	900,000
- Loan Guarantee	7,000,000
	$11,400,000

2. **Sprung Contribution**

- Shareholder Loan	$ 3,500,000
- Loan Guarantee	500,000
	$ 4,000,000

3. **Newfoundland Enviroponics Ltd.**

- Lease/Purchase Agreement for growing lights as arranged by the Sprung Group on behalf of the Company	$ 3,000,000
Total Financing	**$18,400,000**

THE LEGAL AGREEMENTS

The three key legal agreements relating to the joint venture company, Newfoundland Enviroponics Limited, and construction of the Hydroponic Facility were, the Shareholders Agreement, the Construction Contract, and the Technology Transfer Agreement.

(i) Shareholders Agreement

This Agreement between Government, the Sprung Group of Companies (Sprung) and Newfoundland Enviroponics Limited (NEL) details the elements of the arrangement as it related to NEL, its operations and the roles and responsibilities of Government and Sprung. The key elements of the Agreement are noted:

Share Structure

- Class "A" Shares: 1,000 voting shares issued to both Government (represented by Newfoundland Industrial Development Corporation - NIDC) and Sprung.
- Class "B" Shares: 3,500 non-voting shares issued to Government in consideration of its equity contribution of $3,500,000.
- Class "C" Shares: Non-voting shares to be issued to Government at a price of $1,000 per share and equal to the value of the final Retail Sales Tax remission provided to the Company (NEL).

Sprung Contribution

Sprung's equity contribution to NEL was $3,500,000. NEL issued a non-interest bearing Promissory Note to Sprung for repayment of the $3,500,000. Under the note repayment of Sprung's $3,500,000 was subordinated to and subject to payment by NEL of dividends on its Class "A" shares; redemption by NEL of the Class "B" shares held by Government; and for the period commencing five years from the date of redemption of the Class "B" shares from Government, the redemption of Class "C" shares held by Government.

This equity of $3,500,000 was made by way of a set-off against payments due by NEL to Sprung under the Construction Contract. As a result, Sprung received a net amount of $10,825,000 under the Construction Contract and the remaining $3,500,000 referred to in the Construction Contract was retained by NEL as Sprung's contribution to the joint venture company. No up front money was advanced by Sprung.

Redemption of Government Shares

The Shareholders Agreement specified that NEL could purchase, in whole or in part, the Class "B" shares held by Government at their issued price, plus a cumulative annual premium calculated at a rate of prime plus 1%. This option could be exercised to the point where 50% of the shares were purchased, after which all remaining Class "B" shares held by Government must be purchased as a block. Any redemption in whole or in part of Class "B" shares held by Government would include at no additional cost, a redemption of a similar proportion of Class "A" shares.

NEL could also purchase Class "C" shares held by Government in whole or in part, at their issued price, plus the cumulative increase in the consumer price index from the date of issue of the shares to the date of purchase. The redemption or purchase of Class "C" shares had to occur in any event within five years of the date of redemption of the last of the Class "B" shares.

Board of Directors

The Agreement provided for Government and Sprung to jointly appoint a Chairman of the Board of Directors and further provided that Sprung and Government were each entitled to nominate one half of the other members of the Board. Government's Directors were authorized to agree with the appointment of Mr. Philip Sprung as Chairman of NEL.

Management

Under the Agreement, Sprung was given responsibility for the overall management of NEL with Government consent required on specific matters (i.e. annual capital expenditures exceeding $100,000; remuneration and benefits for management employees; the wind-up, liquidation or dissolution of the Company).

Energy Provisions

Sprung was liable for payment of the cost of all energy consumed at the Facility in excess of 26.5 million kilowatt hours per year of electricity or its equivalent in some other energy form. For any year in which the electricity consumed at the Facility was less than 26.5 million kilowatt hours (or its equivalent), Sprung would receive a payment from NEL equal to the amount by which the cost of 26.5 million kilowatt hours exceeded the cost of electricity actually consumed. This was done to ensure that energy costs to NEL would not exceed the level projected by Sprung in his initial proposal. Potential energy consumption was one of the key concerns raised by the Supervisor of Crop Production.

Sprung was also responsible for all electricity consumed by the growing lights and the Agreement included a provision whereby Sprung could recover outlays in this regard from profits in excess of those projected in the pro-forma statements contained in the Agreement.

Working Capital

The line of credit required for the operations of NEL was to be the responsibility of the Company.

Default

The Agreement specified that if Sprung defaulted in the performance of any of its obligations under the Agreement, Government could give notice, following which Sprung would have 90 days to remedy the default. If Sprung failed to remedy the default within this period specific courses of action were available to Government (ie. assume control of the Company, utilize the technology in Newfoundland, etc.). Similar remedies were also available to Sprung in the event of default by Government.

(ii) Construction Agreement

This Agreement between the Sprung Group of Companies (Sprung) and Newfoundland Enviroponics Limited (NEL) provided for the actual construction of the Facility and all site related work. This was a turnkey contract which envisaged the Facility being turned over to NEL when the first crops were planted in all eight production zones. The construction contract provided as follows:

Construction Contract Price	$14,325,000
Land Purchase (NLHC)	150,000
Engineering Services (Dept. of Transportation)	25,000
Total Cost	**$14,500,000**

The Construction Contract was signed on June 25, 1987 and the Facility was substantially completed by April 1988, however, several aspects of the Facility, in particular the lights, were not fully operational until October, 1988.

(iii) Technology Transfer Agreement

This Agreement between Sprung and Government provided for an exclusive, non-assignable license respecting existing and future technology associated with the Sprung Greenhouse System. The license permitted Government to use the technology to operate the Facility and required the joint approval of Sprung to use existing and future technology anywhere else in the Province. In addition, Government was prohibited from further assigning the rights provided by the license and was required to keep confidential all information respecting the license.

OPERATION

During the period leading up to the start-up of the Facility, discussions were held with a number of financial institutions to secure an adequate line of working capital. While the Royal Bank of Canada was prepared, on the strength of the projected receivables and inventory, to provide a line of credit of $300,000, this was not sufficient to cover the projected requirements of NEL. On February 17, 1988, Government approved by (MC 225-'88) a guarantee of $2,000,000 for a working capital line of credit at the Royal Bank over and above the $300,000. Sprung was not able to contribute to the working capital requirements of NEL. As construction of production zones were completed, seeds were planted (initiation) and production eventually came on stream. All zones were either in production or in the initiation stage by April of 1988. Effectively, NEL started to come on stream in May and June of 1988, at a time of year when all domestic greenhouse producers were in the marketplace, an abundance of field grown produce is available, and prices are at their lowest. As a result of these factors, the

Company's working line of credit was depleted by July and Government decided by (MC 1048-'88) to provide a further $2,600,000 guarantee to the Royal Bank for working capital. Based on cash flow projections by management, this amount was supposed to be sufficient to carry the operation to January of 1989 by which time prices and production were projected to be sufficient to sustain the operation.

During early summer of 1988, Sprung had approached Government on a number of occasions indicating his dissatisfaction with the electricity provisions associated with the growing lights. Sprung maintained the growing lights were making a significant contribution towards heating costs at the Facility and, as such, the original agreement between the parties in respect of energy costs should be changed. Government therefore agreed by (MC 1048-'88) to defer enforcement of the energy provisions of the Shareholders Agreement and to allow NEL to pay all energy costs subject to a year end accounting.

Throughout the rest of the summer and into the early fall of 1988 losses continued to mount and by November of 1988, Government had decided by (MC 1426-'88) to provide a further loan guarantee of $825,000 to allow the operation to continue.

After months of disappointing results, a number of weeks of steadily increasing production did occur in November of 1988, culminating in output of about 75,000 cucumbers during the week of November 28 to December 3, 1988. This production level, however, was still insufficient to sustain the operation on an economically viable basis. Early in December of 1988, Sprung Management reported that a catastrophic crop failure appeared to be occurring at the greenhouse. During the week of December 5th to December 10th production fell to about 35,000 cucumbers and the week following to about 10,000 cucumbers. At this stage all the plants were effectively dead. Sprung could not identify with certainty the cause of the crop failure, however, it was advanced that there had been deliberate herbicide contamination of the growing solutions.

Horticulturalists were consulted as to the crop failure and it was suggested that plant symptoms were consistent with herbicide contamination. Enviro-Test Laboratories of Edmonton, Alberta tested plant tissue and confirmed the presence of traces of herbicide in plant tissue. At Government's request, the National Research Council in Halifax attempted to duplicate Enviro-Test's findings utilizing the same tissue samples, however, they were unable to identify any herbicide presence even with the assistance of Enviro-Test's technicians. Government was therefore reluctant to publicly subscribe to the deliberate herbicide contamination theory.

A police investigation was commenced. Herbicides were not used at the Facility and the type of contamination could it was alleged only have occurred through deliberate introduction of the chemical into the growing system. To date results of this investigation have not been released.

To the end of November, 1988, NEL had drawn $4,900,000 in an operating line of credit at the Royal Bank.

In early December of 1988, steps were taken to reduce the workforce at the Facility to minimum levels. All dead plants were removed, the Facility was completely cleaned and the nutrient system flushed. Government decided to provide funding to initiate sufficient planting to replant the Facility in early January of 1989 since at that time a sale of the Facility might be possible. During the period December 22, 1988 to January 27, 1989 a loan of $1,335,000 was made from NIDC to NEL by (MC 1549-'89). This was estimated to be sufficient to cover costs to the end of January of 1989.

SELLING PRICE OF PRODUCT

With respect to the prices NEL secured for its product while under Sprung management, the following presents average month-end prices for the period May to November, 1988. In the months of October and November 1988 NEL was the only domestic producer in the market place and demand was quite strong and resulted in higher prices for the product.

Selling Prices Per Cucumber

May 1988	$0.63
June 1988	0.63
July 1988	0.67
August 1988	0.67
September 1988	0.50
October 1988	0.71
November 1988	0.90

Market information indicated prices continued to escalate during the months of December of 1988, January and February of 1989, apparently reaching as high as $1.50 per cucumber.

FINANCIAL EXPOSURE

Government's financial exposure with respect to NEL, up to the date of the appointment of the Receiver March 3, 1989, was $19,032,000, versus Sprung's exposure of $4,000,000. Details of this exposure are subsequently discussed in this report.

OFFER TO PURCHASE FACILITY

Initial Proposal

In January of 1989, a consortium of Canadian, American and Dutch businessmen communicated to Government their interest in taking over the Facility. Subsequently, however, upon the appointment of the Receiver, the prospective purchasers indicated they were not prepared to proceed to a purchase because of significant capital expenditures required to effectively operate the Facility. Their decision was deferred until the Dutch completed a detailed assessment.

Receivership

Government's initial position with respect to the sale of NEL was that Government and Sprung would both honour their guarantees and liquidate the bank indebtedness of the Company. Subsequently, negotiations between

Sprung and Government for the sale of the Facility broke off such that on February 20, 1989 Sprung advised he was not prepared to enter into a sale transaction.

In response to this, Newfoundland Industrial Development Corporation (NIDC), on February 20, 1989, under approval granted by (M.C. 192-'89), formally demanded payment under its debenture for the $1,335,000 direct loan provided to NEL. Several days after this demand, Sprung agreed to proceed with the sale and instructed NEL's management employees to cooperate fully with the transition to the new owner/manager. Management subsequently refused to cooperate and initiated a series of requests relating to a severance package.

On March 3, 1989, at 1:45 p.m., Government received notice from management employees that they would be walking off the job at 2:30 p.m. and would be staying out until their severance demands were met. At 2:30 p.m. on the same day, Clarkson Gordon were appointed Receiver/Manager of NEL by NIDC and took control of the Facility. Clarkson Gordon subsequently ran the Facility with the assistance of one, and at times two, Dutch technical advisors. Government subsequently approved the provision of a $1,000,000 guarantee on behalf of the Receiver by (MC 242-'89). Funding in the amount of $200,000 for the purpose of paying the receivership and legal costs of NIDC to March 31, 1989, was also approved by (MC 321-'89). Subsequent to the receivership, NIDC used $500,000 of the last $2,200,000 direct loan approved for NEL by (MC 130-'89), to pay off directly the unsecured creditors at the time of receivership.

On March 22, 1989, NEL's contract with New-Land Enterprises Limited, a company incorporated by NEL to supply labour to the Facility, was terminated by the Receiver and all workers at the site then became employed by Clarkson Gordon as Receiver/Manager. The UFCW subsequently applied to the Labour Relations Board for a successor rights order against NEL and Clarkson Gordon Inc. as Receiver/Manager. The application was not opposed and the order was granted.

Dutch Assessment

Shortly after the Facility was placed into receivership, a preliminary report on the status of the operation was provided to Government by the Receiver/Manager and an official of a Dutch Company. The official indicated management of the Facility was, to say the least, flawed. Carbon dioxide was at a level dangerous to the plants, nutrients were being poorly utilized, monitoring of carbon dioxide, nutrients, water, etc. were all manual and insufficient, there was too much algae allowed to accumulate, and, most importantly, the plants were not maintained at near required levels (i.e. trimming and clipping).

Efforts taken to correct some of these deficiencies met with a degree of success. Production results since the receiver took over the Facility are noted:

Production Levels

March 06 - March 11	59,000 cucumbers
March 12 - March 18	85,000 cucumbers
March 19 - March 25	74,000 cucumbers
March 26 - April 01	31,000 cucumbers
April 02 - April 08	16,000 cucumbers
April 09 - April 15	74,000 cucumbers

The decrease in production during the period March 26th to April 8th was caused primarily by two factors. Firstly, propane gas leaks from furnaces in two of the eight zones caused serious damage to mature plants in both zones resulting in reduced output. Secondly, plants that were in production on March 3rd, when the receiver took over the Facility, were not in good condition and the Dutch official felt he had achieved as much economical production from those plants as was possible and decided to remove them from the Facility, to give new plants better lighting and growing conditions. As such, production during the week of April 2nd to April 8th was minimal. The dramatic increase in production during the week of April 9th to April 15th was as a result of new plants in six of the eight zones being in production. While production levels improved, the Dutch official indicated the possibility of future gas leaks represented a serious hazard that had to be addressed if the Facility was to succeed.

While production was still at levels below the initially projected output, it should be noted that the level and consistency of production sustained by the Dutch involvement significantly exceeded anything Sprung management was able to attain on a consistent basis. As well, the Receiver/Manager with the Dutch involvement were able to significantly reduce operating costs through a variety of measures.

CONCLUDING EVENTS

Cabot Produce Inc., a Newfoundland Company, formed from a Canadian, Dutch Consortium subsequently entered into an agreement with Clarkson Gordon Inc. the Receiver/Manager of NEL for the management and operation of the Facility for the period May 1, 1989 to June 30, 1989.

On June 28, 1989 at a public auction the Facility was sold to Government (NIDC a crown corporation) upon a bid of $3,000,000.

Government subsequently entered into an arrangement with Cabot Produce Inc. for the operation and management of the Facility. Subsequently in July of 1990 Cabot Produce Inc. ceased operations and the facilities assets were eventually sold to a Montreal Firm Acier Hurtsteel Canada Limited for the sum of $700,000. Government under the arrangement with Cabot Produce Inc. were to share in the sale proceeds.

Governments involvement in and with the Hydroponic Facility for all intents and purposes was finally at an end.

PART III

THE SPRUNG TECHNOLOGY

The technology put forth by Sprung involved:

Commission Document
[C.D.]

1. Structures covered with a special fabric material that allegedly provided for the optimum use of available light thereby enhancing plant growth;

2. An environment that was strictly controlled by computerization to accurately monitor the ingredients that are necessary for plant growth such as plant nutrients, water and humidity;

3. A system of plant or crop production without the use of soil where plants are placed in plastic funnels through which a solution is continuously recirculated providing plant nutrients precisely and constantly measured. The system was allegedly developed by Girocrop Limited whose main principal was Michael Anselm.

C.D. 006, pp. 053-088

This technology was reputed by Sprung to produce 6.7 million pounds of salad crop (cucumber and tomatoes) during the operations first year with production increasing to 9 million pounds by the fifth year of operations.

C.D. 006, pp. 001-052

From January through to early Spring of 1987, various trips were made to Calgary by an assessment team composed of senior civil servants to assess the Sprung Facility at Calgary and to endeavour to arrive at a financial package that could be considered by Government.

ASSESSMENT OF THE SPRUNG FACILITY AT CALGARY

The Supervisor of Crop Production from the Provincial Department of R.A.N.D. upon his visit to Calgary in February/March of 1987 found no evidence based upon his assessment of the Facility, of the production figures presented to him, that the proposed yield as put forth by Sprung could be obtained under the Newfoundland climate.

The only production yields actually provided were for the limited period from April-August 1986 and indicated approximately 1.3 million pounds of cucumbers were grown during this period. Assuming 100% utilization of the Facility and annualizing the April-August yields, the assessment team projected the Facility could produce 5.4 million pounds of cucumbers. This was a very optimistic projection since production levels would be much lower in winter months because of less light. No production yield was available on tomatoes.

It is to be noted Sprung had no artificial lighting in the production zones of the Calgary Facility. The reason given for the low production yield through April-August of 1986 was caused by start-up problems, natural gas leaks from the heating system, inexperienced staff and refinement of the growing technology, all of which had an adverse effect on production.

Actual production levels for the Operating period September-December 1986 were not received on the basis the results would not have accurately reflected production capacity due to alleged hydrocarbon pollution problems. Sprung did in fact have hydrocarbon problems in March of 1987 which allegedly caused a massive crop failure at the Facility. Other factors, however, have been advanced as to the crop failure, all of which could very well have been consistent with a failure in the technology advanced by Sprung.

C.D. 006, pp. 112-117
C.D. 006, pp. 089-107
C.D. 006, pp. 120-122

SPECIAL FABRIC COVERING

One of the features of the technology advanced by Sprung was that the special fabric covering the structures provided for the optimum use of available light which had a beneficial effect of enhancing plant growth. During the Supervisor of Crop Productions visit to the Facility at Calgary he requested that he be permitted to take light meter readings within the structures to determine if in fact the special fabric had the light enhancing qualities as alleged. He was not permitted to do so in spite of the fact that the Supervisor of Crop Production had executed a Confidentiality Agreement coveting not to disclosure so called trade secrets as had other officials and in spite of the fact that the Sprung technology was patented.

C.D. 001, pp. 114-122
C.D. 006, pp. 053-088

A test conducted for the Commission on an actual sample of the Sprung Fabric to determine its effect on the transmission of light measured in foot candles noted the following:

> A Sekonic Model L-28 exposure (light) meter was used to measure the illumination in foot candles. A cardboard box with a 400 sq. cm opening at the top was used to exclude all light except from the opening. The opening was exposed to outside light during sunny and cloudy conditions. Four readings were taken under both conditions with and without the opening in the box covered with the "Sprung" fabric. The average reduction of light intensity was 69% under sunny conditions and 50% under cloudy conditions.

The test did not indicate that the reduction of light intensity would be similar in a greenhouse covered with the same fabric and tested under similar conditions. What the test showed with regard to the sample of the Sprung fabric tested was that the fabric reduces the transmission of light. Since light is the limiting factor for plant growth during the winter months in Newfoundland, the test would appear to indicate a greenhouse covered with this type fabric as was tested would limit plant growth more than a fabric which was clear.

C.D. 006, pp. 123-127
C.D. 006, pp. 112-117

LIGHTING

It is a fact that light is a critical factor for the economic yield of greenhouse crops including cucumbers and tomatoes. Research has shown that when daily light levels fall below 300 langleys (unit of light measurement) the economics of greenhouse vegetable production is questionable. This situation occurs regularly in Newfoundland from October to March. Given that the light levels in Calgary are much higher than in the St. John's area the Supervisor of Crop Production estimated that a very optimistic annual yield for the Sprung Facility in Newfoundland would be 2.3 million pounds of tomatoes, and 3.1 million pounds of cucumbers and not the yield estimated by Sprung of some 6.7 million pounds. In response while Sprung was not prepared to provide production guarantees, he was, however, initially willing to install growing lights in the Newfoundland Facility and assume the total capital cost of approximately $3,000,000 and associated operating costs of the growing lights. Sprung anticipated that the lights in the Facility could increase production levels by 40-50%. This fact could not be confirmed, however, it was acknowledged that growing lights could have a positive impact on production. It is to be noted Sprung had no artificial lighting in the production zones in the Calgary Facility and his projection of increased production levels as a result of such lighting could not have been based on actual experience.

C.D. 006, pp. 089-107
C.D. 006, pp. 053-088

CONSUMPTION LEVELS

The Sprung proposal estimated Production and Sales for the first year of operation to be 6.7 million pounds of produce of which 4 million pounds would be cucumbers and 2.7 million pounds tomatoes. It was projected that 60% or 4 million pounds of this production would be exported and 40% or 2.7 million pounds would be sold in the Newfoundland market. Information from local wholesalers indicated the total annual consumption levels in Newfoundland for cucumbers and tomatoes would be more in a range of 800,000 pounds and 4.5 million pounds respectively. As to market projections the assessment team concluded the Sprung proposal would have to capture an excess of 50% of the local market if they were to achieve their market projections. This assumption was considered overly optimistic given that cucumbers (English variety-seedless) and greenhouse tomatoes produced at the Facility would be competing with cheaper American type cucumbers and cello-packed tomatoes which represented approximately 90% and 50% respectively of all cucumbers and tomatoes then sold in the province.

C.D. 006, pp. 053-088

MARKET PRICES

The Sprung proposal projected an average price of $1.08 for 6.7 million pounds of produce for the first year of operation. Because of swings dictating price during the various seasons of the year, it was recognized by the assessment team that there was no assurance that the wholesale price would at least be $1.08 as projected in the Sprung proposal.

C.D. 006, pp. 053-088
C.D. 006, pp. 120-122

LABOUR COST

Sprung proposed a much higher labour cost than was common in the industry. The proposal worked out to 24 people for every acre of production area. By comparison, in Ontario some large (8 acre) operations have 3-4 people per acre. In Nova Scotia where there is less labour saving equipment and individual operations are smaller, 6-8 people are required for every acre of production area.

C.D. 006, pp. 089-107
C.D. 006, pp. 118-119
C.D. 006, pp. 108-111

OTHER PROVINCES

It is to be noted, Sprung proposed establishing similar Hydroponic Greenhouses in the Provinces of Quebec and Prince Edward Island which proposals were subject to Federal and presumably some Provincial Government assistance.

The Proposal for the Province of Quebec did not proceed for various reasons one of which was that the proposal was not eligible for Federal Government assistance through various Federal Government programs.

The Proposal for the Province of Prince Edward Island was considered by the Atlantic Employment Program (Federal) and a decision was made at the very latest on December 22, 1986 that the proposal for Prince Edward Island was not eligible for Atlantic Employment Program (AEP) assistance for various reasons one of which was that:

> "the proposal was weak and leaves a lot of questions unanswered pertaining to markets, financing, development costs and demonstration of viability of technology which had not been independently verified".

C.D. 006, pp. 128-129

The Federal Department of Regional Industrial Expansion did not provide financial assistance to the Sprung proposal for Prince Edward Island because of concerns over

> "the long-term viability of the technology involved and of the consequent commercial viability."

C.D. 006, p. 130

It is to be noted the Newfoundland Government obtained copies of two reports on the Sprung Calgary Facility, done for and on behalf of the Prince Edward Island Government. The reports were done in February and March of 1987 by experts who visited the Calgary Facility. While both were impressed by the Calgary Facility and its accoutrements for plant growth, they could not confirm production yields advanced by Sprung nor the technology nor were the economics of such a Facility assessed. Both experts it would appear relied entirely on what was put forth by Sprung as to potential production yields and of the technology relating to such yields, which yields were far, in excess of the norm.

C.D. 006, pp. 131-135

It is noted published reports of "pretty massive uncertainties regarding the Sprung Greenhouse Enterprise" were outlined in the Sunday Express publication of June 14, 1987 some eleven days prior to the signing of the Legal Agreements committing the Province to the project.

C.D. 006, pp. 136-140

It is further noted the report of an official of Holgreeve International B.V. a Dutch company specializing in the ownership and management of vegetable producing greenhouses throughout the world, done as a result of his visits to the Mount Pearl Facility between February 21 - March 3, 1989 indicated amongst other things:

1). That the majority of plants in the preproduction and production zones exhibited signs of poor care and maintenance and that a proper climate was not being maintained for efficient plant growth;

2). That in certain areas algae was found to be growing in the inlets and outlets of the Nutrient Channels as well as in the preproduction zones;

3). The management staff did not meet by far the minimum level required to make the Facility work;

4). The number of people required to produce the expected number of cucumbers would always be much higher than anywhere else;

5). That the material covering the structure was worn out and seriously damaged in certain zones and that small holes in the material allowed water to leak through causing growth of algae on the interior side of the walls;

6). The likelihood of a full crop failure (without immediate proper and necessary changes) by mid March 1989 similar to the crop failure that occurred in December of 1988.

It is further noted that the production record for one week during the operation and management of the Facility by Sprung was considerably less than the production originally forecasted by Sprung.

C.D. 006, pp. 141-146

Findings:

- **that the production yield advanced by Sprung of some 6.7 million pounds of production for the first year of operation could not be confirmed.**

- **that the quality if any, of the special fabric, covering the structures, of enhancing plant growth was not substantiated by light meter readings as it should have been.**

- **that it would appear the fabric as was tested and as heretofore referred to reduces the transmission of light and since light is the limiting factor for plant growth during the winter months in the province, it would appear a greenhouse covered with such fabric as was tested could limit plant growth more than a material which is clear.**

- that the Consumption levels and market price of cucumbers and tomatoes were overly optimistic.

- that the design of the Facility determined a much higher labour cost than was common in the industry.

- that the Sprung technology had not been independently verified.

- that Government failed to properly address the very valid concerns as to the viability of the Sprung proposal raised in the reports of the Supervisor of Crop Production for R.A.N.D. and noted by the rejection of Federal Government assistance for a similar proposal for Prince Edward Island.

- that Government proceeded without adequate, proper and due investigation of the technology and economic viability of the Sprung proposal.

PURCHASE OF THE FACILITY, LAND AND EQUIPMENT

CONSTRUCTION CONTRACT

Article 4.4(b) of the Shareholders Agreement provides that "Sprung shall construct the Facility on the land up to and including the planting of the first crop in production zones of the Facility for a fixed price not exceeding $14,325,000 in accordance with the Construction Contract". On June 25, 1987 NEL, the owner, entered into a Construction Agreement with Sprung Environmental Space Enclosures Ltd. ("SESE") and Sprung Instant Structures Ltd. ("SIS") (collectively known as the Contractor) to construct a Production Facility on the lands owned by NEL for a contract price of $14,325,000. The Production Facility is defined in Article 1.1(g) of the Construction Agreement as "an improvement to be constructed upon the lands to the same specifications, and generally of the same type, standard and quality, as the existing Facility, except to the extent that the parties may specifically agree otherwise". Articles 1.1(k) and (l) of the Construction Agreement define equipment and the existing Facility as that which is in Calgary growing horticultural products in a controlled environment. In 1987 the Contractor relocated the equipment and existing Facility from Calgary to 147 Commonwealth Avenue near Mount Pearl, Newfoundland and with improvements as agreed upon erected the Facility for NEL for the contract price of $14,325,000. It is noted that at a meeting of the Board of Directors of NEL on April 28, 1988 the Board accepted the Substantial Completion date of the Facility, as represented by the Contractor, to be April 06, 1988 subject to deficiencies listed as at April 27, 1988 and that holdback funds be released when available under the Mechanics Lien Period.

C.D. 001, pp. 027-073
C.D. 001, pp. 074-109
C.D. 005, pp. 046-060

It is noted that the Construction Agreement was intended to be a turnkey project for a fixed price and that upon completion of the start up functions outlined in Article 8.6 of the Agreement, care, custody and control, the Facility would pass from the Contractor, to NEL. A major change to the Construction Agreement occurred, without formal amendment to the Agreement, when the parties agreed that initiation and transfer would happen when each production zone came on stream. Costs of maintaining the crop in each production zone would therefore be reimbursed by NEL to the Contractor until such time that all eight zones were initiated. Only after the eighth zone was initiated would the Facility pass to the owner, NEL. The initiation of the eight zones took place during the period December 07, 1987 to April 04, 1988. Labour, energy and other operating costs were prorated during this period by the Contractor to Contractor's costs and to Owner's costs (NEL). The latter being costs associated with the maintenance of the crops during the period December 07, 1987 to April 04, 1988.

C.D. 015, pp. 001-028
C.D. 007, pp. 005-011
C.D. 007, p. 028

The obligation by NEL for the contract price under the Construction Agreement was to be settled as follows:

Due on signing	$ 1,500,000
Due on delivery	4,000,000
Progress payments on Phase I	2,600,000
Progress payments on Phase II	6,225,000
	$14,325,000

C.D. 011, pp. 012-013
C.D. 016, pp. 006-063

The actual distributions made with respect to the contract price are summarized as follows:

Cash payments direct to the Contractor (SESE/SIS)	$ 9,414,580
Transferred to the holdback bank account and ultimately to or for the benefit of the Contractor	1,410,420
Amount withheld from the Contractor and credited to advance by Sprung to NEL	3,500,000
	$14,325,000

C.D. 011, pp. 012-013
C.D. 016, pp. 006-063

Total cash expenditures by NEL on the Facility, land and equipment (excluding the Sylvania high density Lighting System which is addressed in another section of this Report) by period as defined later in this report is summarized as follows:

	Amount	%
Period one	$15,143,235	99.0
Period two	42,307	.1
Period three	-	
Period four	145,369	.9
Period five	-	
	$15,330,911	100.0

C.D. 011, pp. 001-020

No amounts have been deducted from the above cash expenditures for the Investment Tax Credit Refund of $287,684 which is addressed in another Section of this Report. Period one cash expenditures on the Facility, land and equipment were summarized from the accounting prepared by management whereas periods two and four cash expenditures were prepared from the accounting of Commission Accountants and Receiver Manager respectively.

C.D. 005, pp. 066-067
C.D. 010, pp. 081-082
C.D. 009, pp. 001-110

Of the total cash expenditures by NEL on the Facility, land and equipment (excluding the Sylvania Lighting System) the following provides a breakdown between total payments to Sprung related entities as defined vs. payments to third party suppliers:

Total amounts paid to Sprung related entities	$14,510,300
Total amounts paid to third party suppliers	820,611
	$15,330,911

C.D. 011, pp. 017-020

Period one cash expenditures on the Facility, land and equipment are broken down by accounting classifications as follows:

Land	$ 150,000
Land improvements	625,391
Fencing	79,200
Building and structures	13,689,993
Equipment	219,985
Lighting System (other than Sylvania Lighting System)	190,014

Computer Systems	168,485
Furniture, laboratory and generator	20,108
	$15,143,235

C.D. 011, pp. 002-014

Period one cash expenditures on the Facility land and equipment are summarized by supplier source as follows:

Supplier	Description	Amount
SESE/SIS	Facility (Construction Contract)	$14,325,000
NEL	Capitalized interest during construction	374,077
Various suppliers, the majority of which were initially paid by Sprung and reimbursed by NEL	Electrical equipment (other than Sylvania Lighting System)	190,014
Newfoundland and Labrador Housing	Land	150,000
Other	Sundry Equipment	104,144
		$15,143,235

C.D. 011, pp. 002-014

FUNDING OF CAPITAL EXPENDITURES

Article 4 of the Shareholders Agreement sets out the initial funding provisions for NEL. In summary, the following sub-articles are related to the financing of the construction price of the Facility ($14,325,000), the acquisition of land ($150,000) and the engineering services from the Province ($25,000) for a aggregate amount of $14,500,000:

Article	Nature	Amount
4.2/4.5(a)/4.8	Issued Class B Shares to the Province for cash consideration	$ 3,500,000
4.3(a)	Province guarantee of NEL Loan to construct Facility	7,000,000

4.4(a)	Issue of Subordinated Promissory Notes to Sprung for an advance to NEL (offset against progress payments due under Construction Agreement)	3,500,000
4.4(c)	Sprung guarantee of NEL loan to construct the Facility	500,000
		$14,500,000

C.D. 001, pp. 034-037
C.D. 016, pp. 006-063

The actual required funding for the capital expenditures on the Facility, land and equipment by NEL for period one was $15,143,235. Funding of this amount came from the following sources:

Province equity contribution (as per Agreement above)	$3,500,000
Sprung subordinated debt contribution (as per Agreement above)	3,500,000
NEL bank debt guaranteed by the Province (as per Agreement above)(Capital Loan)	6,975,000
NEL bank debt guaranteed by Sprung (as per Agreement above)(Capital Loan)	500,000
	$14,475,000
NEL bank debt secured by additional guarantees of the Province (not provided for in the Shareholders Agreement)(Part of operating loan for $4,900,000)	668,235
	$15,143,235

C.D. 011, p. 002
C.D. 016, pp. 064-080

ENGINEERING SERVICES

Article 7.4 of the Shareholders Agreement makes provision for the payment of $25,000 for engineering services respecting land within sixty days from the Agreement date. This amount is not included in the cash expenditures by NEL for the Facility, land and equipment since the Company never paid the amount to the Province.

C.D. 001, p. 045
C.D. 016, pp. 014-015

CONTRACT PRICE

Initial discussions with Government contemplated a new Facility being purchased from Sprung for a turnkey, contract price of approximately $13,500,000. Government was to provide infrastructure improvements for an additional estimated cost of $1,000,000. As negotiations proceeded between Government and Sprung an existing Facility in Calgary operated and owned by Sprung was substituted for a new one. It is interesting to note that the contract price for the relocation of the existing used Facility and equipment and erection of the Facility in Newfoundland including all infrastructure improvements was $14,325,000. Furthermore, the used Facility meant the loss of approximately $1,175,864 of Investment Tax Credit refunds available to NEL; a source of cash funding in the initial year or two that NEL lost without any offsetting cash compensation being received from Sprung.

C.D. 006, pp. 120-122
C.D. 006, pp. 053-088
C.D. 010, pp. 081-082

Estimates were obtained from other suppliers of greenhouse facilities with comparable production output. A conventional greenhouse estimate of less than $20 per square foot was quoted by an Ontario supplier. Sprung's cost was approximately $41 per square foot. Notwithstanding the inherent weakness in comparing the Sprung Facility to quotations from others, there is the appearance at least that NEL may have paid considerably in excess of market price for a Facility that was purportedly using advanced technology to achieve above normal production volumes. Furthermore, NEL took on the obligation to finance the Sylvania Lighting System, for an additional capital cost of $3,400,000. NEL, not Sprung, was to pay the debenture principal and interest to Sylvania. The additional capital and operating cost for Lighting would support the assertion that NEL probably paid an excessive price for the Sprung Facility.

ENVIRONMENTAL COMPUTER

A cost component of the purchase price of the Facility was the supply of an environmental computer ($106,500) and contract work related to the environmental computer ($29,200) for an aggregate amount of $135,700. Documentation available to the Commission raised serious doubts about the installation and functioning of the environmental computer. Nevertheless, the $135,700 was part of the contract price of $14,325,000 paid by NEL for the Facility purchased from Sprung.

C.D 005, pp. 025-041
C.D. 016, pp. 006-023
C.D. 005, pp. 044-045
C.D. 011, pp. 001-016

The amount of $135,700 is included in period one cash expenditures for Facility, land and equipment in the accounting classification of computer system with a balance of $168,485.

LIGHTING SYSTEM

It is noted that the accounting records of NEL at the end of period one contained an account called Lighting System with a balance of $190,014. Of particular note is that $172,619 of this account balance was paid to SESE, the Contractor, for items purchased by SESE and charged to NEL.

C.D. 011, pp. 001-018

It is noted further that Sprung was not responsible for the cost of the high density Lighting System. NEL entered into a contract to purchase the Lighting System for $3,400,000 from Sylvania. The purchase price was financed by the supplier, Sylvania.

C.D. 007, pp. 002-003
C.D. 011, p. 021
C.D. 001, p. 050

Documentation in the agreements, minutes and records are inadequate to determine why NEL recorded the following capital costs as Lighting System expenditure. These items are grouped by questionable percentage i.e. one hundred per cent questionable expenditure or less than one hundred per cent:

Questionable Expenditures (100%)

Payee	Description/Supplies	Amount
SESE	Labour (Prince)	$ 4,448
SESE	Labour (Prince)	720
SESE	Labour (Prince)	559
SESE	Labour (Prince)	30
SESE	Labour (Prince)	2,410
		8,167
SESE	Breakers (Wesco)	3,876
SESE	Copper rods (Union)	652
SESE	Conduit (Union)	1,023

SESE	Tech (Anixter)	2,357
SESE	Copper stranded (Anixter)	688
SESE	Breaker boxes (Harris & Roome)	7,406
SESE	Generator rental (Ted Cap)	1,800
SESE	(Under $500 amts.)	1,625
		27,594

SESE	Engineering (Cassie)	3,260
SESE	Engineering (Cassie)	2,775
SESE	Engineering (Cassie)	4,268
SESE	Labour of McKay (SESE)	3,333
WESCO	Transformer (Wesco)	16,500
		$ 57,730

Questionable Expenditures (Less than 100%)

Payee	Description/Supplier	Amount
SESE	Stress Cones (Nfld. Power)	$ 1,250
SESE	Terminations (Keough)	1,700
SESE	Terminations (Murrin)	600
SESE	Conductor (Wesco)	6,582
SESE	Switch (Wesco)	66,690
SESE	Cable (Wesco)	22,114
SESE	Equip. hire (Tors Cove)	6,850
SESE	Rock (Tors Cove)	1,020
SESE	Sand (Tors Cove)	3,069
SESE	V Wire (Nfld. Power)	7,500
		$117,375

C.D. 015, p. 009
C.D. 015, pp. 007-011

Of the $117,375 above, it is estimated by the Commission that the amounts do not exclusively relate to the Lighting System and accordingly NEL should have received an allowance for approximately $17,770. This is further discussed later in the report.

C.D. 007, pp. 050-057

RETAIL SALES TAX

Article 4.3(b) of the Shareholders Agreement states that the Government shall provide for the benefit of the Company:

> "a refund of tax paid under the Retail Sales Tax Act by the Company, its agents, contractors and sub-contractors on tangible personal property and services used or consumed solely in the construction and equipping of the Facility for the commencement of operations, all as described in the Construction Contract".

C.D. 001, pp. 034-035

Article 4.5(b) of the Shareholders Agreement states that the Company shall issue out of treasury to Government:

> "in consideration of the refund specified in paragraph 4.3(b) sufficient Class C shares at an issue price of $1,000 per share to equal the value to the Company of the said refund, as determined by auditors designated by Government following completion of construction of the Facility. The said shares shall be issued as fully paid and non-assessable".

C.D. 001, p. 036

Article 4.5 of the Construction Agreement refers to the fact that the Contractor shall be responsible for and shall pay and discharge all Government, sales and other taxes.

C.D. 001, p. 087

It is noted that Class C shares were to be issued by NEL to the Province equal to the refund of Retail Sales Tax. It has been further noted that the Company, contractor, sub-contractor or their agents did not as intended collect Retail Sales Tax on tangible personal property and services used or consumed solely in the construction and equipping of the Facility. The Department of Finance (Retail Sales Tax Division) of the Province did not issue any refunds for Retail Sales Tax paid nor did the Province's auditors undertake an audit for the purpose of verifying the amount. Further, no Class C shares were issued by NEL to the Provincial Government as was required by Article 4.5 (b) of the Shareholder's Agreement.

C.D. 001, p. 035
C.D. 004, pp. 047-048

(MC 692-87) dated May 21, 1987 authorized the necessary amendments to the Retail Sales Tax Regulations to permit an overall exemption to the joint venture with any additional exemption provided pursuant to these amendments to be compensated by the provision of Class B Shares of the joint venture in an equivalent amount.

C.D. 002, p. 004

(MC 853-87) dated July 7, 1987 provided for the remission of Retail Sales Tax to Sprung Instant Structures in accordance with the Shareholders Agreement and the Construction Agreement and pursuant to Section 19 of the Financial Administration Act with such remission to be made upon application and subject to The Honourable The Minister of Finance receiving any information he deems necessary respecting an application.

C.D. 004, pp. 001-002

It is to be noted that Retail Sales Tax had to be paid by all companies involved in the construction of the Facility including NEL at the time of purchase. NEL was supposed to apply to the Department of Finance for a refund of tax it paid. The Department of Finance as indicated received no application for refunds and therefore no refunds were made.

C.D. 004, pp. 047-048

It is to be noted contractors (subcontractors) could subsequently directly apply for Retail Sales Tax refunds for Retail Sales Tax paid on materials and equipment purchased and which became part of the Facility.

C.D. 004, p. 049

It is also noted subcontractors were subsequently authorized to deduct Retail Sales Tax paid from their progress billings to the contractor and did also offset the Retail Sales Tax paid against their monthly Retail Sales Tax Account to the Department of Finance.

C.D. 004, p. 050
C.D. 004, p. 051

It is further noted confusion existed as to whether there was an overall Retail Sales Tax exemption with regard to the construction of the Facility or whether Retail Sales Tax had to be paid in the normal course of events and an application made for a refund of the Retail Sales Tax paid.

C.D. 004, p. 052

Substantial Completion of the Facility occurred in April of 1988 or at the very latest in October of 1988.

C.D. 005, p. 046
C.D. 005, pp. 062-065

Findings:

- **that there is inadequate policy guidelines available to ascertain the fairness of the charges by the Contractor to NEL for the Lighting System in the amounts of $57,730 and $17,770.**

- **that 95% of the cash expenditures for Facility, land and equipment were paid to Sprung.**

. that the Province guaranteed a bank loan for NEL to fund capital expenditures in period one in the amount of $668,235 which was not part of the funding set out in the Shareholders Agreement. No formal amendment to the Agreement was undertaken for this matter. Article 14.2 stated that the line of credit necessary for the Company's operations was to be the responsibility of the Company.

. that the provision of $25,000 for engineering services rendered by the Province was never paid by NEL.

. that the Company, in paying $14,325,000 for the Facility, and taking on the obligation for a high density Lighting System at a cost of $3,400,000, would appear to have paid an excessive price in 1987 for a Facility that was purportedly using advanced technology to achieve above normal production volumes.

. that the Company paid $135,700 for an environmental computer system as a cost component of the contract price for the Facility, which may never have been installed and therefore was never functional.

. that there is insufficient documentation in the agreements, minutes and records of the Company to determine that charges by the Contractor to NEL together with a purchase from a third party arranged by the Contractor for the Company for Lighting System equipment aggregating $75,500 were proper capital expenditures of the Company and therefore were proper and authorized payments by the Company.

. that according to the cash expenditures there was a duplicate payment by the Company for a conductivity meter in the amount of $2,337. Payments were made to the supplier and to SESE, the Contractor.

. that the intent of Article 4.3 (b) of the Shareholders Agreement was that Retail Sales Tax where payable was to be paid by all companies/contractors, and subcontractors involved in the construction of the Facility including the owner

Newfoundland Enviroponics Limited at the time of purchase. The owner would eventually apply to the Department of Finance for a refund of the Retail Sales Tax paid by it and the Retail Sales Tax paid by the owner to the Contractor.

- **that subsequently contractors and subcontractors could apply for Retail Sales Tax refunds directly to the Department of Finance.**

- **that confusion prevailed regarding the Retail Sales Tax. No applications were made by the owner (NEL) for a refund of Retail Sales Tax paid. Instances of sub-contractors using their own tax exempt number to purchase materials then subsequently calculating the Retail Sales Tax and deducting same when billing the contractor, as well as subcontractors paying Retail Sales Tax, then offsetting the amount paid against their monthly account to the Department of Finance, occurred.**

- **that there was no set firm determinable policy as to Retail Sales Tax and no accurate records to indicate the extent of the Retail Sales Tax paid if at all by all contractors/ subcontractors.**

- **that Article 4.5 (b) of the Shareholders Agreement states that in consideration of the refund (of Retail Sales Tax) sufficient Class C shares at an issue price of $1000 per share to equal the value to the Company of the said refund would be determined by auditors designated by Government following completion of construction of the Facility. No audit was under taken to determine the value of the Class C Shares following completion of construction of the Facility.**

- **that no class C shares were issued by the Company pursuant to Article 4.5(b) of the Shareholders Agreement.**

PART IV

SPRUNG ACCOUNTING

An accounting of the sources and uses of cash for the Sprung Greenhouse Project was prepared by Commission Accountants for the period 1987 to 1989.

The accounting records of NEL available to Commission Accountants were incomplete. The Commission found it necessary to obtain certain accounting information from third party sources in order to prepare the Sources and Uses of Cash Statement. Third party sources for this purpose included entities such as Banks, Suppliers, External Auditors, Receiver Manager, Government Agencies, etc.

Commission Document Basic Financial System (BFS) contains the computerized accounting detail in support of the Sources and Uses of Cash Statement. Commission Accountants prepared BFS from their review and analysis of (a) the cash receipts and cash disbursements transactions as recorded in the bank statements for NEL, (b) the records of the Receiver Manager for NEL, and (c) schedules of direct payments on behalf of NEL by the Provincial Government and or its Agencies. Third party information obtained by the Commission was also used to prepare this accounting. Commission Accountants have undertaken a compilation engagement and not an audit engagement and therefore are unable to express an opinion as to whether the Source and Uses of Cash Statement is complete in all respects.

The financial statements prepared by NEL as at November 30, 1988, were converted to a cash basis of accounting with reference to data contained in NEL records and in the External Accountants audit working papers. The receipts and disbursement transactions for NEL for the period subsequent to November 30, 1988 were accumulated and summarized by Commission Accountants. All of this data was processed by Commission Accountants through BFS to arrive at the Sources and Uses of Cash Statement for NEL for the period 1987 through 1989.

ACCOUNTING PERIODS

The sources and uses of cash have been accumulated through the use of five distinctive groupings, described as five accounting periods. These five accounting periods are defined as follows:

- **Period One** Represents the cash transactions in NEL from the start of the Project (1987) to November 30, 1988, the financial reporting year end for NEL.

- **Period Two** Represents the cash transactions in NEL for the period December 01, 1988 to the first week of March, 1989 the time of the appointment of a Receiver Manager for NEL.

- **Period Three** Represents cash payments made by the Provincial Government subsequent to March 03, 1989 (the date of Receivership of NEL) for creditor claims on NEL outstanding as at March 03, 1989.

- **Period Four** Represents the cash transactions of the Receiver Manager while NEL was in Receivership (including the activities of Cabot Produce Inc.)

- **Period Five** Represents all remaining cash transactions not grouped in either of the above four periods (i.e. includes the repayment of NEL bank loans with the Royal Bank).

Periods one and two relate to the time that NEL was under the direction of the Management team for the Company. Period three relates to a distinctive activity initiated by the Province; that is the payment of creditor claims on NEL as at the date of the Receivership for goods and services provided to NEL prior to the Receivership. Period Four covers the period of Receivership of NEL (including the activities during the time that Cabot Produce Inc. was being monitored by the Receiver Manager). Period five relates to activities where it was not practical to group them into one of the other four accounting periods.

C.D. 009, pp. 001-110
C.D. 016, pp. 064-077

Findings:

- that the accounting records of NEL made available to the Commission were incomplete.

- that regular financial statements for NEL, other than those at November 30, 1988, were not available to the Commission.

- that the external auditors reporting under date of April 04, 1989 were unable to express an opinion as to whether the financial statements of NEL for the period ended November 30, 1988 were presented fairly in accordance with generally accepted accounting principles.

- that the financial statements of NEL for the period ended November 30, 1988 contained note disclosure that "the possibility exists that the company may be unable to continue realizing its assets and discharging its liabilities in the normal course of business."

SOURCES AND USES OF CASH STATEMENT

A summary of the cash transactions for the Sprung Greenhouse Project has been prepared and is described as the Sources and Uses of Cash Statement. This statement covers the period commencing in 1987 when the Project was under the direction of Mr. Sprung through to March 03, 1989 when Newfoundland Enviroponics Limited ("NEL") was placed in receivership by the Province. The statement also includes the operations of the Project while under the direction of the Receiver Manager through to late summer of 1989. Detailed analysis of the compilation of the Sources and Uses of Cash Statement can be found in Commission Document Basic Financial System. Also contained in the Commission Document Basic Financial System is an analysis of the Sources and Uses of Cash by period (the accounting periods are defined in other sections of this Report).

The Sources and Uses of Cash for the Project are summarized as follows:

NEWFOUNDLAND ENVIROPONICS LIMITED
Sources and Uses of Cash Statement
Sprung Greenhouse Project

1987 to 1989

Sources of Cash	
Government of Newfoundland investment and advances	$22,208,021
Sprung Group investment and advances	4,000,000
Sale of Produce	1,166,871
Investment tax credit refund	327,830
Cabot and Holgreeve advances	344,306
Interest received on funds in holdback account	88,900
Other receipts	59,584
TOTAL SOURCES OF CASH	**$28,195,512**

Uses of Cash

Purchase of Greenhouse Facility, equipment, and land (except Sylvania Lighting System)	$15,330,911
Payments on Sylvania Lighting System debenture	552,409
Payments from interest earned on holdback account	88,900
Advance to Cabot Produce Inc.	500,000
Receivership professional fees and expenses	695,905
	17,168,125
Operating expenditures:	
Wages and benefits	3,586,613
Seeds, nutrients, hydrocanal, blocks, lab supplies, and analysis	1,003,344
Electricity	1,878,294
Propane	539,891
CO2	85,411
Water	157,291
Packaging, shipping, customs	448,109
Repairs, maintenance and rentals	303,000
Contractors and consultants	228,600
Insurance	82,408
Professional fees	159,089
Security	107,091
Telephone	52,893
Travel	54,817
Interest and bank charges	1,918,547
Other expenditures	421,988
Total operating expenditures	**11,027,386**
TOTAL USES OF CASH	**$28,195,512**

C.D. 009, pp. 001-110

Findings:

- **that the Province funded the Sprung Greenhouse Project in the amount of $22,208,021 which accounted for approximately 80% of the total sources of cash for the Project. The Shareholders Agreement contemplated the province financing the Project in the following manner:**

Equity	$ 3,500,000
Loan guarantee	7,000,000
	$10,500,000

- that in addition to the above financing the Shareholders Agreement contemplated a remission of Retail Sales Tax by the Provincial Government relating to the construction of the Facility and acquisition of equipment amounting to $900,000. No remission of Retail Sales Tax (the amount has never been quantified) is included in the funding of $22,208,021 referred to above.

- that the Sprung Group contributed $4,000,000 to the Sprung Greenhouse Project which accounted for approximately 15% of the total sources of cash for the Project. The Shareholders Agreement contemplated the Sprung Group contributing the following financing for the Project:

Shareholder loan	$ 3,500,000
Loan guarantee	$ 500,000
	$ 4,000,000

- that $3,500,000 of the Sprung Group contribution was a direct "set-off" against progress payments due to Sprung by NEL under the Construction Agreement.

- that the financial risk associated with the Project was almost entirely with the Province notwithstanding that NEL was a joint venture between the Province and the Sprung Group.

- that the total cash collected from sales of produce by the Project amounted to approximately $1,166,871 for the initial eighteen months operations during 1988 and 1989 whereas the forecasts (June 1987) for the Project showed sales revenue of $8,090,250 for the first twenty months of operations.

- that the Investment Tax Credit ("ITC") refund from the Federal Government was $287,684 whereas the forecasted (June 1987) amount was $1,552,000 based on the assumption that NEL would receive a new Facility.

. that the total uses of cash for the Project aggregated $28,195,512 for the period 1987 through 1989 which was disbursed, in a summary form, as follows:

. Purchase of Facility, land and equipment (excluding Sylvania Lighting System)	$15,330,911
. Payments on Sylvania Lighting System debenture	552,409
. Operating expenditures (including interest but excluding depreciation)	11,027,386
. Receivership costs and other	1,284,806
	$28,195,512

. that approximately 61% ($17,297,000) of the above uses of cash for the Project were disbursed to the Sprung Group, including the entities known as Mecanico Construction Limited and New-Land Enterprises Limited, for Capital Expenditures on Facilities and Operating Expenditures during the period 1987 through 1989.

. that the Sylvania Lighting System debenture for $3,400,000 was paid down by $345,586 (principal and interest payments totalled $552,409) as of the date of receivership, March 03, 1989. No further payments were made by NEL and Sylvania had the Lighting System removed.

. that the excess of operating cash expenditures over operating cash receipts for the Project for the period ended March 03, 1989 (date of receivership of NEL) was $8,174,301; that is a net operating cash loss of $8,174,301. The forecast in June 1987 attached to the Shareholders Agreement showed that the Facility was projected to generate sales revenue of $8,090,250 during

the first twenty months of operations, have operating expenses of $7,417,986 and generate a positive cash flow of $672,264 before income taxes and debt repayment. The Project fell far short of the forecasted financial performance and in fact never showed any operating economic viability during any sustained period of operations.

GOVERNMENT OF NEWFOUNDLAND
INVESTMENT AND ADVANCES

On June 25, 1987 the Province and Sprung incorporated a jointly-owned company Newfoundland Enviroponics Limited ("NEL") to construct and operate a Facility in Newfoundland for use in the cultivation, production, processing and marketing of horticultural products and related research and development. C.D. 001, p. 033

C.D. 001, pp. 027-073
C.D. 001, pp. 074-109
C.D. 001, pp. 114-122

The Province and Sprung, as owners of NEL, entered into a Shareholders Agreement, a Construction Agreement and a Technology Transfer Agreement on June 25, 1987 respecting the operations and functioning of NEL, construction of the Facility and the technology.

Funding of the initial capital cost of the Facility is addressed in the Shareholders Agreement and is summarized as follows:

Province equity contribution	$ 3,500,000
Sprung subordinated debt contribution	3,500,000
NEL debt guaranteed by the Province	7,000,000
NEL debt guaranteed by Sprung	500,000
	$14,500,000

C.D. 001, pp. 034-035

Article 4 of the Shareholders Agreement relating to the financial contribution of the Province towards the initial capital funding of the Facility is summarized below:

4.1 "The Class 'A' shares shall be owned equally by Sprung and Government, subject to the provisions of this Agreement respecting the transfer or redemption of Shares"

4.2 "Government shall transfer the sum of $3,500,000 to the Company"

4.3 "Government shall further provide for the benefit of the Company:

(a) a guarantee to a commercial lending institution on terms and conditions satisfactory to Government of a $7,000,000

> loan to enable the Company to construct the Facility."

4.5 "The Company shall issue out of treasury to Government:

> (a) in consideration of matters specified in paragraph 4.2 (a) and (b) 3500 Class 'B' shares as fully paid and non-assessable".

4.6 "In consideration of the other benefits provided by the Shareholders to the Company pursuant to this clause and to the other terms and conditions of this Agreement the Company shall:

> (a) issue out of treasury to Government 1000 Class 'A' shares as fully paid and non-assessable."

C.D. 001, pp. 034-037

Articles 9 and 10 of the Shareholders Agreement address the responsibility of Sprung and NEL for the cost of electricity and energy used by the Facility. These provisions will be addressed in other sections of this report.

C.D. 001, pp. 048-053

It is noted in Article 14.2 of the Shareholders Agreement:

> "The line of credit necessary for the Company's operations will be the responsibility of the Company."

C.D. 001, p. 055

Soon after commencement of operations early in 1988 NEL required cash to fund its negative working capital needs arising out of ongoing operating losses. Notwithstanding Article 14.2 of the Shareholders Agreement, wherein it was contemplated that the line of credit necessary for operations would be the responsibility of NEL, the Province found it necessary to guarantee additional operating bank loans for the Company. That is, additional to the $7,000,000 guarantee for the initial capital cost of the Facility provided for in Article 4.3 of the Shareholders Agreement and approved by (MC 692-'87) of May 21, 1987. These additional loan guarantees by the Province, as provided for in Minutes of Council, are as follows:

Feb. 17, 1988 (MC 225-'88)	$ 2,000,000
July 14, 1988 (MC 1048-'88)	2,600,000
Nov. 17, 1988 (MC 1426-'88)	825,000

Mar. 10, 1989 (MC 242-'89)	1,000,000
May 30, 1989 (MC 403-'89)	500,000

Further, the Province provided funding to NIDC who in turn advanced funds to NEL, for the company to pay its operating losses. Details of the Minutes of Council are as follows:

Dec. 22, 1988 (MC 1549-88)	$ 1,335,000
Feb. 08, 1989 (MC 130-'89)	2,200,000

C.D. 002, pp. 001-069
C.D. 010, pp. 001-033
C.D. 016, pp. 081-087

In addition, by way of (MC 321-'89) the Province provided funding of $600,000 for professional fees and for unsecured creditors of NEL as at March 03, 1989.

Findings:

- **that the Province funded the capital cost of the Facility acquired by NEL and its operating losses through into 1989 in the aggregate of $22,208,021.**

- **that the Province funded the working capital requirements of NEL arising primarily from operating losses notwithstanding that the line of credit necessary for the Company's operations was to be the responsibility of NEL in accordance with the provisions of the Shareholders Agreement. It is to be noted that Sprung did not share in this funding notwithstanding that NEL was a joint venture.**

- **that the Province funded net cash operating losses of $8,174,301 for the period from commencement of operations early in 1988 to March 03, 1989, the date NEL was placed in receivership by the Province. According to the forecast done for NEL, a positive cash flow was expected for the first twenty months of operations not a negative cash flow.**

- **that the Province funded the capital cost of the purchase of the initial Facility and the cost of equipment purchases through to March 03, 1989, the date of the receivership of NEL, in the amount of $10,857,713** whereas the Shareholders Agreement contemplated a maximum funding of $10,500,000. Much of the additional equipment cost of $357,713 funded by the Province was for equipment purchased by NEL through Sprung. Included in this additional equipment is an amount of $75,500 which appears to be a questionable capital cost of NEL. This matter is subject to additional commentary in other sections of this report.

- that as of March 03, 1989, the date of receivership of NEL, the Province's funding for the Project aggregated $19,032,014 whereas Sprung's funding aggregated $4,000,000.

GOVERNMENT FUNDING BY PERIOD

The Province's funding for the Greenhouse Project has been summarized into five accounting periods (as defined in other sections of this Report) as set out below:

NEWFOUNDLAND ENVIROPONICS LIMITED
Sources of Cash
Government of Newfoundland Investments and Advances
Summary Schedule

1987 - 1989

Period one	
Issue of Class B shares by NEL to NIDC for cash	**$ 3,500,000.00**
Period two	
Cash advances from NIDC to fund NEL operations	**2,935,000.00**
Period three	
Pre-receivership amounts funded by NIDC and/or Government Departments	**604,450.10**
Period four	
Funding from NIDC for operations of Receiver	**1,264,440.57**
Period five	
Funding from Government to pay out loans with RBC	10,136,378.53
Funding by NIDC for purchase of Greenhouse Complex (net of Expenses)	2,899,677.00
NIDC/Government funding for professional fees and expenses	695,904.62
Funding from Government for advance to Cabot Produce	500,000.00
	14,231,960.15
Less ITC refund and interest	- 327,829.87
	13,904,130.28
Total Government of Newfoundland Investments and Advances	**$22,208,020.95**

C.D. 010, pp. 001-033

Findings:

- that in Period One, NEL issued Class 'B' shares to NIDC in exchange for $3,500,000 in cash which was received by NEL during the period October 13, 1987 through to December 14, 1987. An analysis of the Project Construction Costs, Financing and Distributions shows that the $3,500,000 received by NEL over the period October 1987 to December 1987 was used to finance in part the Construction price of the Facility. The issue of Class 'B' shares for cash was provided for in Articles 4.2 and 4.5 (a) of the Shareholders Agreement. The financial statements of NEL as at November 30, 1988 disclose the 3500 Class 'B' shares as issued and outstanding for a consideration of $3,500,000.

- that in Period Two, the Province advanced cash to NEL for the period December 01, 1988 through to March 03, 1989 in the amount of $2,935,000. This amount consisted of eight cash transfers during the period for funding of operating costs of NEL such as payments to Sylvania for the Lighting System, wages, seeds, electricity, propane, interest, etc.

- that in Period Three, the Province honoured and funded payments totalling $604,450 to creditors of NEL as at March 03, 1989, the date of receivership of the Company. These payments represent operating expenditures of NEL up to March 03, 1989.

- that in Period Four, the Province provided funding for the net expenditures of the Receiver-Manager for NEL aggregating $1,264,441.

- that in Period Five, the Province provided funding for NEL in the amount of $13,904,130 for the following:

(a) Payout of Royal Bank Loans - $10,136,378. On August 18, 1989 NEL's indebtedness to the Royal Bank was paid out of the Province's funding as follows:

Capital loan Facility	$ 4,555,093
Operating loan Facility	5,150,000
Interest (June 26 to Aug. 17)	431,285
	$10,136,378

The capital loan balance at April 12, 1989 of $7,475,000 was repaid as follows:

April 13, 1989 Sprung deposit	$ 500,000
June 20 - 30, 1989 Province/ NIDC deposit	2,419,907
August 18, 1989 Province deposit (above)	4,555,093
	$ 7,475,000

(a) When NEL could not repay its capital and operating loans, the Royal Bank called on the Province and Sprung to honour their guarantees of the loans in the amounts of $6,975,000 and $500,000 respectively. The loan guarantees were in accordance with Articles 4.3(a) and 4.4(c) of the Shareholders Agreement.

(b) NIDC Purchase of the Greenhouse Complex - $2,899,677. NIDC purchased the Greenhouse Complex from NEL with funds provided by the Province. Net proceeds of sale of $2,899,677, after paying costs of disposal in the amount of $100,323, were used by NEL for a payment on the capital loan of $2,419,907 as per (a) above and to pay interest outstanding as at June 25, 1989 of $479,770.

(c) Funding for Professional fees and expenses - $695,904. The Province funded (a) professional fees of the Receiver-Manager for NEL for $477,647, (b) professional fees and expenses for the purchase of the Greenhouse Facility from NEL $100,323 (above) and (c) legal fees related to the above of $117,934 for an aggregate amount to June 1990 of $695,904.

(d) Funding of Advance to Cabot Produce Inc. - $500,000. The Province funded Cabot Produce Inc. in the amount of $500,000 for working capital purposes.

(e) Investment Tax Credit - Receipt of $327,829. The Province (on behalf of NEL) received the proceeds of the Investment Tax Credit in April 1990 in the amount of $287,684 plus interest of $40,146 for a total of $327,829.

SPRUNG GROUP
INVESTMENT AND ADVANCES

Subsections of Article 4 of the Shareholders Agreement relating to the financial contribution of Sprung towards the initial capital cost of the Facility are as follows:

Article 4.4 states Sprung shall:

(a) "advance by way of loan to the Company $3,500,000 as evidenced by a Promissory Note or Notes in the form annexed hereto as Schedule 'A'",

(b) "construct the Facility on the land up to and including the planting of the first crop in pre-production zones of the Facility for a fixed price not exceeding $14,325,000 in accordance with the Construction Contract",

(c) "provide a guarantee to a commercial lending institution on terms and conditions satisfactory to the Shareholder for a $500,000 loan to be obtained by the Company for construction of the Facility."

C.D. 001, pp. 034-035

Article 4.6 states that in consideration of the other benefits provided by the Shareholders to the Company pursuant to this clause and to the other terms and conditions of this Agreement the Company shall:

(b) "issue out of treasury to Sprung 1000 Class 'A' shares as fully paid and non-assessable".

C.D. 001, p. 036

Articles 9 and 10 of the Shareholders Agreement address the responsibilities of Sprung and NEL for the cost of electricity and energy at the Facility. This subject will be addressed in other sections of this Report.

C.D. 001, pp. 048-053
C.D. 012, pp. 104-150

It is noted in Article 14.2 of the Shareholders Agreement:

> "The line of credit necessary for the Company's operations will be the responsibility of the Company."

C.D. 001, p. 055
C.D. 010, pp. 033-036

Findings:

- that Sprung funded the capital cost of the Facility acquired by NEL in the amount of $4,000,000 as follows:

  (a) an amount of $3,500,000 was withheld from progress payments due to Sprung under the Construction Agreement for the purchase and erection of the Facility acquired by NEL.

  (b) an amount of $500,000 was contributed by Sprung and applied by the Royal Bank on April 13, 1989 to reduce the capital loan in the name of NEL. This transaction was in accordance with the guarantee given by Sprung under Article 4.4(c) of the Shareholders Agreement.

- that the funding contribution of $3,500,000 was a "self-financing" transaction by virtue of the fact that Sprung had the proceeds from the Construction Agreement to finance the advances required under the Shareholders Agreement.

- that the financial statements of NEL for the period ended November 30, 1988 report a "subordinated promissory note, payable to Sprung Sales Limited and Sprung Environmental Space Enclosures Limited, without interest" in the amount of $3,500,000.

- that Sprung did not share with the Province in the funding of the operating losses of NEL which aggregated $8,174,301 for the period ended March 03, 1989 the date of receivership of NEL. The Shareholders Agreement, which created NEL as a joint venture between the two parties, provided in Article 14.2 that "the line of credit necessary for the Company's operations will be the responsibility of the Company". It appears that after the initial funding was in place, the two parties, that being Sprung and the Province, would share in any future or additional financial risk that may arise with regard to NEL. This principle was not adhered to since the Province funded the operating losses of $8,174,301 to March 03, 1989. These losses were not shared by Sprung.

SALES OF PRODUCE

The Shareholders Agreement (3.2) stated that the purpose of the Company included the following: the cultivation, production, processing and marketing of horticultural products; research and development related to the cultivation, production, processing and marketing of horticultural products; and the performance of all matters necessary or desirable in connection with the foregoing.

C.D. 001, p. 033

Actual sales and sundry revenue achieved by the Project were $1,166,871 while sales and sundry revenue for the period ended March 3, 1989 amounted to $858,673.

C.D. 010, pp. 031-033
C.D. 010, pp. 037-080

Prior sections of this Report addressed the technology put forth by Sprung and outlined its alleged advanced features for the growing of salad crops such as cucumbers and tomatoes. The Sprung process was alleged to be able to produce 6.7 million pounds of salad crop during the first year of operation with production levels increasing to 9 million pounds by the fifth year of operation. Sprung forecasted that the average selling price of crops produced at the Facility during the first year would be approximately $1.08 per pound. On forecasted production levels of 6.7 million pounds at an average selling price $1.08, NEL was forecasted by Sprung to generate sales volume of approximately $7,236,000 in its first year of operation.

C.D. 006, pp. 053-088

Findings:

- **that cash sales for the Project, a period of approximately eighteen months (commencing in February, 1988 and ending with the Receiver Manager in mid 1989), amounted to $1,166,871.**

that the cash sales and sundry revenue for the period ended March 03, 1989 (approximately thirteen months) amounted to $858,673. This level of sales activity was generated during the period that the Facility was under the control of management and

during a time when Mr. Sprung was Chief Executive Officer of NEL.

- **that the actual sales for the Project fell far short of the forecasts put forth by Sprung and the Company (i.e. first year sales put forth by Sprung were forecasted to be $7,236,000; and the first twenty months sales for the Project per Schedule B to the Shareholders Agreement were forecasted to be in excess of $8,000,000).**

- **that Government did not take proper steps to independently investigate the technology, the production capability of the Project and the marketability of the production output to substantiate the sales forecasts and therefore, the economic viability of the Project.**

INVESTMENT TAX CREDIT REFUND

An Investment Tax Credit ("ITC") refund of $1,463,549 was accounted for in the financial statements of NEL for the period ended November 30, 1988 as a receivable and as a reduction in the cost base of the applicable assets as set out in Note 4 to those financial statements. This accounting was considered to be in accordance with generally accepted accounting principles by those who prepared the financial statements.

C.D. 016, pp. 064-077

In preparing the ITC Return (T2038) for the Company for the period ended November 30, 1988 an ITC refund was claimed in the amount of $1,463,549. Under the Income Tax Act an ITC refund may be claimed under certain circumstances when a Company incurs qualified expenditures and those expenditures meet the prescribed criteria set down under the Act. One of the criteria is that the asset has not been previously used or previously acquired for use or lease for any purpose whatsoever.

C.D. 010, pp. 081-082

It is to be noted that the financial advisors to the Company believed, based on their analysis of the information and physical inspection of the Facility, that an "aggressive filing position is warranted and can be professionally justified". It is further noted, however, that in Revenue Canada's opinion "the relocation of the Facility to Newfoundland does not satisfy the substantially new concept and the Facility should be regarded as used property and therefore not qualified for ITC". Revenue Canada only allowed certain component parts of the Facility such as the "Lighting System (Sylvania)" as qualified expenditures for ITC purposes and disallowed the basic Facility on the basis that it had been used before.

C.D. 005, pp. 066-067

Accordingly, Revenue Canada reduced the ITC refund to $287,684 from that claimed by the Company in the amount of $1,463,549. Interest of $40,146 was allowed by Revenue Canada bringing the total receipt by the Province on behalf of NEL to $327,830 in April, 1990.

C.D. 010, pp. 081-082

It is to be noted that the projected income statement and cash flow appended as Schedule B to the Shareholders Agreement forecasted an ITC cash refund of $1,552,000 to be received during the second fiscal period of operations. It is recognized, however, that Investment Tax Credits is one of the items mentioned in Article 10.7 of the Shareholder's Agreement that is to be "finalized" for purposes of the Cash Flow Projection attached to the Shareholder's Agreement. Nevertheless, the Company was budgeting for a much larger ITC refund than that actually received of $287,684.

C.D. 001, pp. 071-073
C.D. 010, pp. 081-082

Article 12.1 of the Shareholders Agreement states that:

> "If the investment tax credit or any other taxable benefits available to the Company under the Income Tax Act (Canada) are reduced because components from Sprung's SESE System Facility in Calgary, Alberta are installed in the Facility, Sprung will pay an amount equal to such reduction from the sum received by Sprung from any settlement of, or judgement relating to, claims for damages arising from the necessity to close the SESE System Facility in Calgary, Alberta. Sprung will assign this portion of the benefits of any such settlement or judgement to the Company."

C.D. 001, p. 054

Findings:

- **that the cash flow to the Project from the ITC refund was reduced significantly from that forecasted i.e. actual receipt of $287,684 vs. forecast amount of $1,552,000.**

- **that neither NEL nor Government received the deficiency in cash flow of $1,175,864 from the reduced ITC refund as was contemplated in the Shareholders Agreement (deficiency calculated as the ITC refund claimed on the T2038 less the actual ITC refund received from Revenue Canada).**

- **that the Province failed to obtain an independent tax opinion on the impact that a used Facility would**

have on the forecasted ITC refund of $1,552,000 and whether there was reasonable assurance that the refund amount claimed would be realized through receipt.

- **that a claim exists against Sprung (Sprung Sales Limited and or Sprung Environmental Space Enclosures Limited) for $1,175,864 conditional upon Sprung receiving damages arising from the necessity to close the SESE system Facility in Calgary, Alberta.**

INTEREST ON LIEN HOLDBACK ACCOUNTS

Article 4.2 of the Construction Agreement (as amended) sets out the payment schedule for the Contract Price of $14,325,000 for the initial purchase and erection of the Facility. C.D. 001, pp. 110-112

Article 4.3 of the Construction Agreement with regard to Lien Holdbacks reads as follows:

> "The payments referred to in Section 4.2 shall be subject to the withholding of such sums for such minimum periods of time as are required under Applicable Laws in respect of builders 'or mechanics' liens and all sums so held back shall promptly be paid to the Contractor immediately upon becoming releasable to the Contractor under Applicable Laws."

C.D. 001, p. 086

The above Article makes no provision for paying interest on any funds held in a holdback bank account.

Amounts were deposited into a NEL holdback bank account at the Royal Bank equal to 10% of the progress payments due to the Contractor (Sprung). Payments into the account took place during the period August 1987 through to April 1988 and accumulated to $1,410,420. This amount was short of 10% of the contract price of $14,325,000 by $22,080 since there was an offsetting overpayment of a like amount on the contract price.

During the period that funds were on deposit in this bank account at the Royal Bank, interest accrued to a total of $88,900. Likewise, NEL was incurring an interest cost on the bank financing that was incurred to fund the amounts on deposit in this holdback bank account.

A summary of the transactions through the holdback bank account in the name of NEL at the Royal Bank for the period August 1987 through to January 1989 is as follows:

Holdback deposits	$1,410,420
Interest income accrued	88,900
	$1,499,320

Payments out:

Date	Payee	Amount	
May 06, 1988	SESE Ltd.	$ 585,420	
Nov. 18, 1988	SESE Ltd.	803,320	
Dec. 12, 1988	Stirling, Ryan in trust for for SESE Ltd.	75,000	
Jan. 23, 1989	SESE Ltd.	35,580	
		$1,499,320	**$1,499,320**
			0

C.D. 011, pp. 022-025
C.D. 010, pp. 085-088
C.D. 016, pp. 006-063

Findings:

- **that the interest accrued of $88,900 was paid to the Contractor, Sprung or paid for his benefit, notwithstanding that there was no provision in the Construction Agreement to make such payments to the Contractor.**

- **that $75,000 of the interest referred to above was used to settle a claim by Tors Cove Excavating Limited against the Contractor, Sprung.**

- **that NEL incurred an unnecessary interest cost while funding the deposits in the holdback bank account since the interest income earned on the holdback bank account did not accrue to the benefit of NEL.**

WAGES AND BENEFITS

Cash expenditures for wages and benefits for the Project were $3,586,612 which were accounted for by period as follows:

Period one	$2,108,153
Period two	662,591
Period three	136,810
Period four	679,058
Period five	-
	$3,586,612

C.D. 012, pp. 001-065

In period one, an amount of $407,403 (19%) was accounted for as management salaries, including departmental management.

C.D. 012, p. 006

Of the cash expenditures of $3,586,612 for wages and benefits, approximately 51% was paid to Sprung and two labour shops as follows:

SESE	$ 658,893
Mecanico	194,735
New-Land	994,098
	$1,847,726

C.D. 012, p. 004

The Construction Agreement was never formally amended to reflect the major change which occurred when it was agreed that initiation and transfer would take place as soon as each production zone came on stream and that the Contractor would be reimbursed for labour and other maintenance costs for the crops, by the owner subsequent to the initial planting, until all eight zones were initiated at which time the Facility would pass to the owner.

C.D. 007, pp. 005-011

Sprung presented one cost schedule for labour and other maintenance costs to the Board for reimbursement by NEL. These costs represented an allocation of labour between the Contractor and NEL. The Board accepted the cost schedules with the belief that further review and discussion would take place with regard to NEL's responsibility for their share of the costs. It is noted that the initiation for the eight production zones took place during the period December 07, 1987 to April 04, 1988. Additional costs were reimbursed by NEL to Sprung which were not presented to the Board for approval.

C.D. 003, pp. 010-016
C.D. 007, pp. 028-031
C.D. 015, pp. 001-130

C.D. 001, pp. 071-073

It is to be noted that the projected income statement and cash flow attached as Schedule B to the Shareholders Agreement projected production and management salaries for the Company for the first twenty months of operation to be $1,794,167.

Findings:

- **that the Company was remiss in not ensuring that a clear and concise policy was agreed upon by the parties with regard to the fair allocation of labour costs between the Contractor and the owner before the costs were paid by the owner to the Contractor.**

- **that it was next to impossible for the Board of Directors of NEL to monitor the fairness of the allocation of labour costs without a formal amendment to the Construction Agreement reduced to writing.**

- **that wages and benefits for the Project of $3,586,613 were more than three times the revenue from sales for the same eighteen month period.**

- **that wages and benefits for the Project of $3,586,613 for the eighteen month period were double the projected production and management salaries for the Company for the first twenty months of operation.**

PACKAGING, SHIPPING AND CUSTOMS

It is noted that the Company incurred cash expenditures on packaging, shipping and customs in the amount of $322,466 to March 03, 1989, the date of receivership of NEL, while sales and sundry revenue for the same period was $858,673. This expenditure was approximately 37% of the revenue for the same period. C.D. 010, p. 031

The projected income statement and cash flow attached as Schedule B to the Shareholders Agreement showed a packaging and distribution cost of $529,300 on projected sales revenue of $8,090,250 or approximately 6% cost to sales revenue. C.D. 001, pp. 071-073

Finding:

- **that the ratio of packaging, shipping and customs at 37% of sales and sundry revenue was extraordinarily high and far in excess of the projected ratio of 6%. The Company experienced an enormous cost overrun in this expense category and the Province failed to monitor the cost pattern to take action on a timely basis.**

PAYMENTS TO SPRUNG ENVIRONMENTAL SPACE ENCLOSURES LIMITED, MECANICO CONSTRUCTION LIMITED, NEW-LAND ENTERPRISES LIMITED

It is to be noted that the Company made payments to SESE, Mecanico and New-Land aggregating $17,112,931 during the period ending February 22, 1989. An analysis of the payments shows that the following amounts were distributed to:

SESE	$15,345,002
Mecanico	208,030
New-Land	1,559,899
	$17,112,931

It is to be noted that payment of the above amount to SESE was for the following:

Construction Agreement	$14,325,000
Reimbursement for electrical equipment purchases allocated labour costs and other operating expenses	1,020,002
	$15,345,002

The accounting for the payments shows the $17,114,931 being paid for the following:

Property and equipment: Building and structures - Construction Agreement	$14,325,000
Property and equipment Lighting System	172,619
Property and equipment: Other	11,316
	$14,508,935
Wages and benefits	$ 2,384,323
Administration fees	8,305
Worker's Compensation	34,197
Other operating supplies	177,171
	$17,112,931

As other parts of this report show there were no formal amendments made to the Shareholders Agreement or the Construction Agreement, except for one amendment to the latter with regard to payments under Article 4.2(iii) and (iv) of the Construction Agreement. However, a major change in the Construction Agreement took place upon agreement of the parties wherein the initiation and transfer of the crops would take place as soon as each production zone came on stream. The Contractor would be reimbursed its costs of maintaining each crop by the owner (NEL) subsequent to the initial planting, until all eight production zones were initiated at which time the Facility would pass to the owner. Costs related to the maintenance of the crops during the initiation of the eight production zones during the period December 07, 1987 to April 04, 1988 are included in the figure of $1,020,002 set out in the above paragraph.

It is to be noted that no formal executed agreement existed between NEL and the two labour shop companies, namely Mecanico and New-Land for the reimbursement by NEL of labour costs, administration fees and other operating costs. Costs accumulated by Mecanico and New-Land in the amounts of $208,030 and $1,559,899 respectively were paid by NEL. C.D. 015, pp. 001-002

New-Land was incorporated on the 4th day of July A.D. 1988. The incorporators were, a senior management employee of Newfoundland Enviroponics Ltd. and the Company's (New-Land's) legal counsel. The registered office of the Company was the office of its legal counsel. C.D. 005, pp. 124-130

SESE, the contractor, purportedly had an agreement with a company called Mecanico whereby the latter supplied the necessary labour for construction of the Facility. C.D. 005, pp. 131-136

Mecanico was incorporated on the 26th day of August 1987. The incorporators were the same two persons who were the incorporators of New-Land. The registered office of the Company was the same as that of New-Land's. The President of the Company was the same person who was President of New-Land. C.D. 005, pp. 137-144

New-Land was to supply labour services to NEL for operation of the Facility upon employment terms and labour rates payable, as purportedly agreed to between New-Land and NEL.

A draft Agreement between NEL and New-Land existed whether it was in fact executed is unknown.

It is to be noted in the draft Agreement, Newfoundland Enviroponics Ltd. is referred to as N.F.L.D. Ltd. and New-Land Enterprises Ltd. as N.E.L. C.D. 005, pp. 145-152

New-Land's obligations to NEL were carried out, for part of the period of its existence, at the Facility in Mount Pearl, where all payroll files were kept pertaining to the workers employed by New-Land. During the latter part of 1988 New-Land obtained an office in the basement of the residence of an employee of NEL. Subsequent to that period, a further payroll was complied at a house rented by senior management employees of NEL. C.D. 005, pp. 154-155

At a Board of Directors meeting of NEL on April 28, 1988 the issue as to whether NEL was to contract for labour services was discussed and a proposal for same, subject to cost effectiveness was to be presented to the Board subsequently. C.D. 005, pp. 047-059

At a Board of Directors meeting of NEL on November 10, 1988 the Board was notified by Philip Sprung that New-Land had contracted with NEL to provide labour for the operation. It was further noted that the contract would continue but that both companies would accept any union certification order to be made by the Labour Relations Board. C.D. 005, pp. 156-163

It is also noted that the purpose and cost effectiveness of such a contract was never brought before the Board nor was the matter pursued at the Board meeting of November 10, 1988 as it should have been nor was a formal contract executed between the parties.

It is noted no mark-up was to be charged on the services New-Land provided to NEL. Yet the sum of $8,305.43 was paid by NEL to cover expenses of New-Land.

It is significant to note the similarity in the initials or abbreviation of both companies and the fact employee pay cheques of New-Land had in bold print the initials N.E.L. C.D. 005, p. 153

Findings:

- **that the formal policy guidelines under which NEL would accept charges from SESE, Mecanico and New-Land were not in place and that the Province was remiss in not ensuring that such policies were reduced to writing by way of formal Agreement between the parties.**

- **that the Province was unable to ascertain the fairness of charges to NEL from SESE, Mecanico and New-Land aggregating $2,787,931 without written policy guidelines approved formally by the joint venture owners.**

- **that according to the accounting for payments to related parties, NEL paid Mecanico twice for an amount of $22,940 on July 08, 1988 (cheque number 258) and again on August 03, 1988 (cheque number 458).**

- **that according to the accounting for payments to related parties, NEL paid Mecanico on August 03, 1988 an amount of $30,682 for wage adjustments relating to previous errors in six payrolls during the period March 19, 1988 to July 08, 1988.**

- **that according to the accounting for payments to related parties, NEL paid New-Land $8,305 for administration fees to cover expenses during the period September 07, 1988 to February 22, 1989 which were not paid in accordance with any formal Agreement between the parties.**

- that according to the accounting for payments to related parties, the payment on January 10, 1988 by NEL to New-Land for administration fees was for $5,000 whereas the invoice from New-Land shows the administration fee to be $500.

- that according to the accounting for payments to related parties, a duplicate payment may have been made by NEL to SESE for the purchase of chemicals from Van Waters & Rogers in the amount of $9,232. Support for the payment was a purchase order in one instance and an invoice in another instance.

- that New-Land Enterprises Ltd. served no useful function. Its primary purpose was to circumvent any attempt at unionizing the employees at the Facility by inferring that the majority of employees (production workers) were employed by NEL when they were not.

- that subsequently, the matter was resolved when the union brought application for certification before the Labour Relations Board which application eventually applied to both NEL and New-Land.

- that New-Land was an additional cost to NEL when it should not have been.

PART V

LEGAL AGREEMENTS and GOVERNMENTS $3.5 MILLION EQUITY

C.D. 001, pp. 027-073
C.D. 001, pp. 074-109
C.D. 001, pp. 114-122

The Shareholders Agreement, the Construction Agreement and the Technology Transfer Agreement were executed on the June 25, 1987.

It is noted by Article 4.2 of the Shareholders Agreement:

C.D. 001, p. 034

> "Government shall transfer the sum of $3.500,000 to the Company" (Newfoundland Enviroponics Limited).

C.D. 002, p. 004

By (MC 692-87) dated May 21, 1987 government provided that its $3,500,000 equity infusion would flow through NIDC and approved a $7,000,000 loan guarantee on behalf of Newfoundland Enviroponics Limited.

C.D. 004, pp. 001-002

By (MC 853-87) dated July 7, 1987 government authorized execution of the said Shareholders Agreement by The then The Premier and Ministers of R.A.N.D. and Finance; authorized execution of the said Construction Contract by the Company (Newfoundland Enviroponics Limited); and authorized execution of the said Technology Transfer Agreement by The then The Premier and the Minister of Development and Tourism.

C.D. 004, p. 053

By (MC 854-87) dated July 7, 1987 Government ordered that NIDC be authorized to borrow up to $3,500,000 to facilitate its equity investment in the Sprung Group Project and that the Minister of Finance be authorized to provide a Loan Guarantee of up to $3,500,000 on behalf of NIDC.

C.D. 004, p. 003

By (MC 1118-87) dated September 29, 1987 government authorized a special warrant for NIDC equity investment of $3,500,000. MC 854-87 was rescinded.

C.D. 004 pp. 004-046

Section 28(3) of the Financial Administration Act RSN 1973 as amended reads as follows:

If, when the Legislature is not in session, or when the House of Assembly has stood adjourned for more than thirty days, any expenditure not foreseen and not provided for by the Legislature in respect of a new service is urgently and immediately required for the public good, then, upon the report of the Minister that there is no legislative provision and of the Minister having charge of the new service in question that in his opinion the necessity is urgent, giving reasons for his opinion, and that if such expenditure is not made, grave damage to the interests of the Crown or the public will result from delaying the expenditure until the necessary legislative provision has been made, the Lieutenant-Governor in Council may, on the recommendation in writing of the Board, order

(a) that a special warrant be prepared for signature by the Lieutenant-Governor for the issue of the amount estimated to be required, and an additional subhead be set up in the books of the Comptroller against which expenditure on the new service shall be charged; or

(b) if countervailing savings are available from other subheads of the Head of Expenditure concerned, that an additional subhead be set up in the books of the Comptroller to which such countervailing savings can be transferred and against which expenditures on the new service shall be charged, and if the countervailing savings are less than the amount estimated to be required that a special warrant be prepared for signature by the Lieutenant-Governor for the issue of an amount equal to the difference between the countervailing savings and the estimated amount, and such amount shall be added to the additional subhead of the relevant Head of Expenditure.

Findings:

- **that the Execution of the Shareholders Agreement on June 25, 1987 by Newfoundland Industrial Development Corporation and Her Majesty the Queen in Right of the Province of Newfoundland therein collectively called "Government" was without the proper authority of the Lieutenant Governor-in-Council.**

- that the Execution of the Construction Contract on June 25, 1987 by Newfoundland Enviroponics Limited therein called the "owner" was without the proper authority of the Lieutenant Governor-in-Council as required by Article 7.1 (ix) of the Shareholders Agreement.

- that the Execution of the Technology Transfer Agreement on June 25, 1987 by Her Majesty the Queen in Right of the Province of Newfoundland therein called "Government" was without the proper authority of the Lieutenant Governor-in-Council.

- that it is difficult to justify the authorization of a special warrant for the $3,500,000 equity infusion when one considers section 28(3) of the Financial Administration Act 1973 as amended, as to whether the expenditure was foreseen and in respect of a new service; urgently and immediately required for the public good and that if such expenditure is not made grave damage to the interests of the Crown or the public will result from delaying the expenditure, until the necessary legislature provision has been made.

PART VI

LOAN GUARANTEES

GUIDELINES

C.D. 002, pp. 001-003

To provide provincial loan guarantees to companies/corporations through the then existing legislation pertaining to such loan guarantees, certain guidelines were established by government through (MC 84-'85 and MC 951-'85) by which requests for financial assistance were to be considered.

The guidelines established by government through (MC 84-'85) were that requests for assistance be on the following basis:

(a) the request is from an established company in the resource based sectors;

(b) Government's intervention be recognized on all sides as an interim measure only. rather than a means of securing Government's on going participation in the business venture;

(c) the request be to support a working capital line of credit additional to reasonably available bank credit, but not for acquisition purposes, etc.;

(d) the company requesting assistance must strictly comply with the following established criteria for evaluating proposals, i.e. viability, management and demonstrated need;

(e) In regard to security for Government's Guarantees,

   (1) where the "social impact" is considered to be a determining factor, the matter should be referred to a special committee for review;

   (2) as a matter of course, personal guarantees and cross guarantees, if appropriate, should be requested;

   (3) otherwise, the company should have sufficient assets to provide adequate security; and

(4) where companies seeking extensions to their guarantees have improved their financial performance, the Province should seek a reduction in its guarantee;

(f) with the exception of interim extensions of 2 and 3 months for purposes of data preparation, no extensions to guarantee will be given until the Province has received the required documentation similar to that normally provided for new guarantee applications.

C.D. 002, pp. 001-002

The guidelines established by government through (MC 951-85) were succinctly that the authority granted pursuant to the Loan and Guarantee Act 1957 as amended should not be used to

C.D. 002, p. 003

> "supply risk capital assistance to a venture".

Finding:

. that Government ignored the established guidelines/conditions for the granting of loan guarantees to Newfoundland Enviroponics Limited and that the company met at the very most only one guideline/condition, that of demonstrated need.

LOAN GUARANTEES TO JUNE 30, 1989

Governments Loan Guarantees to June 30, 1989 were:

(1). By (MC 692-'87) dated May 21, 1987 government provided a loan guarantee of $7,000,000 to Newfoundland Enviroponics Limited (the joint venture company composed of Sprung and Government for the operation of the greenhouse Facility).

C.D. 002, p. 004

This guarantee was perfected by an Indenture dated July 8, 1987 wherein Government guaranteed to the Royal Bank of Canada $7,000,000 as a result of the Bank's advancing by way of first mortgage $7,500,000 to Newfoundland Enviroponics Limited (Sprung was to provide a Guarantee for $500,000).

Paragraph 5 of the Guarantee Agreement reads:

C.D. 002, pp. 005-010

> "The guarantor (government) covenants and agrees to introduce legislation ratifying this indenture at the next session of the House of Assembly".

C.D. 002, p. 011

The third session of the Fortieth General Assembly sat for the period March 2 - June 19th, 1987.

C.D. 002, p. 012

The fourth session of the Fortieth General Assembly sat for the period March 10 - July 8, 1988.

C.D. 002, pp. 013-021

The loan guarantee of $7,000,000 provided by (MC 692-'87) was not ratified by the House of Assembly until June 30, 1989.

Findings:

- **that the loan guarantee of July 8, 1987 should have been brought before the House of Assembly at the very latest during the fourth session of the Fortieth General Assembly which sat for the period March 10 - July 8, 1988.**

- **that Government not only ignored the convention of bringing Loan Guarantees before the House of Assembly at its next session, Government breached its covenant to the Royal Bank for failing to bring the $7,000,000 Loan Guarantee before the House of Assembly for ratification during the fourth session of the Fortieth General Assembly which sat March 10 - July 8, 1988.**

(2). By (MC 1425-'87) dated December 17, 1987 government provided a loan guarantee of $825,000 to the Royal Bank on behalf of Sprung Environmental Space Enclosures Limited (SESE) the

C.D. 002, p. 022 contractor for an operating line of credit to expire 30 days after the completion of the construction contract.

This Guarantee was perfected by a Guarantee between Government and the Royal Bank dated December 29, 1987.

Paragraph 5 of the Guarantee Agreement reads:

> "The Government covenants and agrees to introduce legislation to amend the schedule to the Loan and Guarantee Act 1957 as amended at the next session of the House of Assembly".

C.D. 002, pp. 023-026

The next session of the House of Assembly was the fourth session of the Fortieth General Assembly which sat through the period March 10-July 8, 1988. C.D. 002, p. 012

(3). By (MC 225-88) dated February 17, 1988 government provided a operating credit loan guarantee of up to $2,000,000 on behalf of Newfoundland Enviroponics Limited to the Royal Bank in addition to all other guarantees previously approved. C.D. 002, p. 027

The said guarantee was secured by an indenture between Government and the Royal Bank dated February 17, 1988.

Paragraph 5 of the Guarantee Agreement reads:

> "The Government covenants and agrees to introduce legislation to amend the Schedule to the Loan and Guarantee Act 1957 as amended at the next session of the House of Assembly in order to perfect this Guarantee".

C.D. 002, pp. 028-032

The next session of the House of Assembly was the fourth session of the Fortieth General Assembly which sat through the period March 10-July 8, 1988. C.D. 002, p. 012

Finding:

. that Government ignored convention and breached its covenant to the Royal Bank for failing to bring the guarantee of February 17, 1988 before the House of Assembly during the fourth session of the Fortieth General Assembly (next session) for ratification.

(4). By (MC 571-88) dated May 2, 1988 this loan guarantee on behalf of the contractor was extended from April 21, 1988 to June 30, 1988. Further extensions to November 30, 1988 were granted by the Bank at the request of Government. C.D. 002, p. 033

This extension to the Guarantee was perfected by an Agreement between Government and the Royal Bank dated the day of May 1988. C.D. 002, pp. 034-036

Paragraph 5 of the Guarantee Agreement reads:

> "The Government covenants and agrees to introduce legislation to amend the Schedule to The Loan and Guarantee Act 1957 as amended at the next session of the House of Assembly". C.D. 002, p. 025

The next session of the House of Assembly was the fourth session of the Fortieth General Assembly which sat through the period March 10-July 8, 1988. C.D. 002, p. 012

Finding:

. that Government ignored convention and breached its covenant to the Royal Bank for failing to bring the Loan Guarantee of December 29, 1987 before the House of Assembly during the Fourth session of the Fortieth General Assembly (next session) nor was the extension to the original guarantee dated May 2, 1988 brought before that session of the House of Assembly.

(5). By (MC 1048-88) dated July 14, 1988 government provided an increase in the operating credit loan guarantee to Newfoundland Enviroponics Limited by $2,600,000, to expire December 21, 1988 with a maximum draw down by September 30, 1988 not to exceed $1,500,000.

C.D. 002, p. 037

This guarantee was perfected by an indenture between Government and the Royal Bank dated July 15, 1988.

Paragraph 6 of the Guarantee Agreement reads:

> "The Government covenants and agrees to introduce legislation to amend the Schedule to The Loan and Guarantee Act, 1957, as amended, at the next session of the House of Assembly, in order to perfect this Guarantee."

C.D. 002, pp. 039-043

The next session of the House of Assembly was the First Session of the Forty-first General Assembly which sat through the period May 21, 1989 to June 30, 1989.

C.D. 002, p. 044

(6) By (MC 1426-88) dated November 17, 1988, Government provided an additional Loan Guarantee of $825,000 on behalf of Newfoundland Enviroponics Limited subject to such conditions as may be required by the Honourables the Ministers of Finance and Justice.

C.D. 002, p. 045

This Guarantee was perfected by a guarantee between Government and the Royal Bank dated December 6, 1988.

Paragraph 5 of the Guarantee Agreement reads:

> "The Government covenants and agrees to introduce legislation to amend the schedule of the Loan and Guarantee Act, 1957, as amended, at the next session of the House of Assembly, in order to perfect this Guarantee."

C.D. 002, pp. 046-050

The next session of the House of Assembly was the First Session, of the Forty-first General Assembly, which sat through the period May 24, 1989 to June 30, 1989. C.D. 002, p. 044

(7). By (MC 1534-88) dated December 20, 1988, Government authorized the Minister of Finance, under authority of the Loan and Guarantee Act, to extend to December 31, 1989, the operating credit guarantees issued on behalf of Newfoundland Enviroponics Limited under Orders-in-Council 225-88, 1049 (48)-88 and 1428-88. C.D. 002, p. 051

These extensions were perfected by an Extension of Guarantee Agreements between Government and the Royal Bank dated January 20, 1989. C.D. 002, pp. 052-053

Paragraph 5 of the Guarantee Agreement (225-88) reads:

> "The Government covenants and agrees to introduce legislation to amend the Schedule to The Loan and Guarantee Act, 1957 as amended, at the next session of the House of Assembly, in order to perfect this Guarantee". C.D. 002, p. 031

Paragraph 6 of the Guarantee Agreement (1048-88) reads:

> "The Government covenants and agrees to introduce legislation to amend the Schedule to The Loan and Guarantee Act, 1957, as amended, at the next session of the House of Assembly, in order to perfect this Guarantee". C.D. 002, p. 042

The next session of the House of Assembly was the First Session, of the Forty-first General Assembly, which sat through the period May 24, 1989 to June 30, 1989. C.D. 002, p. 044

(8). By (MC 242-89) dated March 10, 1989 Government ordered pursuant to the provisions of the Loan and Guarantee Act a loan guarantee to Clarkson and Gordon Inc. as receivers of Newfoundland Enviroponics Limited on behalf of the Government of Newfoundland and Labrador of up to $1,000,000 for working capital requirements, subject to such terms and conditions as may be required by the Honourables, the Minister of Finance, Rural, Agricultural and Northern Development and Justice.

C.D. 002, p. 054

This Guarantee was perfected by an Indenture between the Government and the Royal Bank dated March 10, 1989.

Paragraph 5 of the Guarantee Agreement reads:

> "The Government covenants and agrees to introduce legislation to amend the Schedule to The Loan and Guarantee Act, 1957, as amended, at the next session of the House of Assembly, in order to perfect this Guarantee".

C.D. 002, pp. 055-059

The next session of the House of Assembly was the First Session, of the Forty-first General Assembly, which sat through the period May 24, 1989 to June 30, 1989.

(9). By (MC 403-89) dated May 30, 1989 Government ordered pursuant to the Loan and Guarantee Act a further Loan Guarantee to the Royal Bank of Canada in the amount of $500,000 in favour of Clarkson Gordon Inc. Receiver Manager of Newfoundland Enviroponics Limited on such terms and conditions as the Departments of Finance and Justice deem appropriate.

C.D. 002, p. 060

This Guarantee was perfected by a guarantee between Government and the Royal Bank dated June 02, 1989.

Paragraph 5 of the Guarantee Agreement reads:

> "The Government covenants and agrees to introduce legislation to amend the Schedule to The Loan and Guarantee Act, 1957, as amended, at the next session of the House of Assembly, in order to perfect this Guarantee."

C.D. 002, pp. 061-065

The next session of the House of Assembly was the First Session, of the Forty-first General Assembly, which sat through the period May 24, 1989 to June 30, 1989.

The Loan Guarantees Authorized by:

- MC 692-'87 for $7,000,000
- MC 225-88 for $2,000,000
- MC 1048-88 for $2,600,000
- MC 1426-88 for $825,000 (with the exclusion of MC 1425-87 for $825,000 dated December 17, 1987 and MC 571-'88 dated May 2, 1988. This Guarantee expired without the required amendment to the Loan and Guarantee Act.)
- MC 242-89 for $1,000,000
- MC 403-89 for $500,000

were brought before the first session of the Forty-First General Assembly which sat through the period May 25 - June 30, 1989 and were perfected by the appropriate amendment to the Schedule to the Loan and Guarantee Act 1957 as amended on June 30, 1989.

C.D. 002, pp. 013-021

Finding:

. that the new administration properly bought the heretofore referred to guarantees before the first season of the Forty First General Assembly for ratification.

PART VII

CHANGES TO: CONSTRUCTION AND SHAREHOLDERS AGREEMENTS

The Construction Agreement (Contract) as documented and executed on June 25, 1987 envisaged a turnkey agreement, the Hydroponic Greenhouse Facility being constructed in accordance with the plans and specifications relating to the Facility as it existed in Calgary and being formally passed over to the owner Newfoundland Enviroponics Limited (NEL) after initiation and transfer, the planting of the first crop in preproduction zones (4) and their transfer to production zones (8).

C.D. 001, pp. 074-109

The only formal change to the Construction Agreement occurred when the Construction Agreement was amended on September 24, 1987 which amendment was approved by the Lieutenant Governor-in-Council, was reduced to writing and executed by the parties and related to payments under Article 4.2 (iii) and (iv) of the Construction Agreement.

C.D. 001, pp. 110-113

A major change to the Construction Agreement occurred when it was agreed that initiation and transfer would take place as soon as each production zone came on stream and that the contractor would be reimbursed its costs of maintaining each crop, by the owner (NEL) subsequent to the initial planting, until all eight production zones were initiated, at which time the Facility would pass to the owner.

C.D. 003, pp. 010-016
C.D. 007, pp. 001-011

A major change to the Shareholders Agreement related to the Lease for Lights purchase pursuant to Article 10.1 of the Shareholders Agreement (S.A.). Certain electrical costs as well as other costs were charged back to the owner (NEL) by the contractor, on the basis presumably that such electrical costs related to the growing lights and were not included in the Lease for Lights purchase. This major change was presumably based on the fact that the contractor (Sprung) would not be responsible for any costs relating to the growing lights although the matter was never

C.D. 003, pp. 010-016
C.D. 007, pp. 029-031

discussed or approved at the Board level or by Government.

Article 10.1 of the Shareholders Agreement provided that:

> "Sprung will be solely responsible for the acquisition and installation of the Lights and for arranging a lease for the Company for this purpose in the approximate amount of $3,000,000 no later than the completion date as defined in the Construction Contract. The terms and conditions of the lease will be in accordance with the purchase order executed on June 11, 1987 by GTE Sylvania Canada Limited and subject to the consent of Sprung and the Government".

Article 10.2 of the Shareholders Agreement provided for:

> "the lease to be arranged by Sprung for the Company (NEL), under paragraph 10.1 may provide a first fixed charge on the Lights for the benefit of the lessor".

C.D. 001, p. 050

It is noted a purchase order issued on behalf of a Newfoundland Corporation to be Incorporated, for Lights and for the installation of same with GTE Sylvania Canada Limited for delivery, no later than October 1, 1987 and for installation of the Lights, to be completed by December 1, 1987 at a price of $3,000,000, was executed on behalf of the Newfoundland Corporation to be Incorporated, by two individuals on June 5, 1987, one of whom was P.D. Sprung and was accepted by GTE Sylvania Canada Limited on June 11, 1987.

C.D. 007, p. 001

It is further noted Newfoundland Enviroponics Limited (NEL) by purchase order 0001 issued to GTE Sylvania Canada Limited for the supply and installation of Growing Lights for a contract price of $3,400,000 financed by Sylvania over a seven year period at an annual interest rate of 13% was executed by Newfoundland Enviroponics Limited on September 30, 1987 and accepted by Sylvania Canada on October 11, 1987. Sylvania was to supply labour and materials for the installation of the Growing Lights.

C.D. 007, pp. 002-003

Two payments of $180,900 were acknowledged by Sylvania and a new repayment schedule was agreed upon whereby regular quarterly payments would be $190,609 commencing on March 01, 1990. Three payments of $190,609 were to be made in 1989 with the first on February 15, 1989. The final payment was due in March 1995.

The financial statements of NEL for the period ended November 30, 1988 reflected the Lighting System as a capital asset addition of $3,400,000 and a debenture payable of $3,219,100. The Sources and Uses of Cash Statement shows the cash payments of $552,409 as a Use of Cash and does not reflect the capital asset of $3,400,000 nor the outstanding balance on the debenture. Following the Receivership of NEL on March 03, 1989 the Lighting System was removed by Sylvania.

The above mentioned purchase order formed the basis of the Lease for Lights purchase referred to in Article 10.1 of the Shareholders Agreement with quarterly payments subsequently agreed upon.

C.D. 007, p. 004

It is further noted Jaeger Electric Limited an Alberta Company had a contract with GTE Sylvania Canada Limited for labour for the installation of the growing lights at a price of $971,108. Jaeger Electric Limited subcontracted the installation of the lights to Delta Electric Limited a Newfoundland Company.

It is to be noted no formal agreement in writing set forth the obligation of the contractor (SESE) and the owner (NEL) as it related to each's responsibility as a result of these major changes to the Construction Agreement and Shareholders Agreement.

At a Board of Directors Meeting of NEL held on November 6, 1987 reference is made by the Chairman P.D. Sprung respecting the transfer of title pursuant to the construction contract and who summarized the position to be that:

C.D. 007, pp. 005-011

> "the Company (NEL) would take responsibility for the units as the same were completed and initial plantings done.

At a Board of Directors Meeting of NEL held on December 4, 1987 Dawn Sprung advised that:

C.D. 007, pp. 012-017

> "initial planting of seeds for production would begin on December 7 or 8th".

At a Board of Directors meeting of NEL held on February 10, 1988 reference is made to the matter of transferring operational costs from Sprung to NEL once production zones were seeded. Ms. Sprung noted that:

> "adequate information exists to clearly indicate what costs are construction related versus operational".

Mr. Farquharson (the Contractors Controller and a Board Member of NEL) was requested to prepare a submission dealing with this issue.

C.D. 003, pp. 022-026

At a Board of Directors Meeting of NEL held on February 19, 1988 P. Sprung presented a Cost Summary Analysis and a Staff Employment Summary. Extensive discussion followed respecting the following issues:

(a) The desirability of capitalizing certain costs, for example the electrical costs;

(b) Refusal of Newfoundland Light and Power to cover certain normal installation costs;

(c) Whether NEL should assume costs after planting in each zone;

(d) Whether employment allocations were agreeable given the limited number of zones now in production.

Following discussion, it was unanimously resolved to accept the Cost Summary presented

> "subject to further discussion and review respecting NEL's takeover of production zones and liability for costs prior to initial planting".

C.D. 003, pp. 010-016

At a Board of Directors Meeting of NEL held on March 15, 1988 reference is made by the Chairman P.D. Sprung as to production:

> "P. Sprung outlined the existing situation. Production is now underway in zone 8 with production being provided between cucumbers and tomatoes. Zone 1 is scheduled to have completion of the alpha line next week and in the following weeks pre-production will begin in zone 1 for transfer to zones 2, 3 and 4. Other zones will then be brought into production on a phase basis depending upon the finalization of construction. The last zones are scheduled for late April/early May."

C.D. 007, pp.018-027

It is noted the initiation for the eight production zones took place on the following dates:

1st Initiation	December 7, 1987
2nd Initiation	February 9, 1988
3rd Initiation	March 4, 1988
4th Initiation	March 26, 1988
5th Initiation	March 26, 1988
6th Initiation	March 26, 1988
7th Initiation	April 4, 1988
8th Initiation	April 4, 1988

C.D. 007, p. 028

It is noted that the matter of NEL taking responsibility of the units (production zones) as each zone was completed and the initial plantings done, first arose at a Board Meeting of NEL on November 6, 1987.

It is further noted that the first initiation (planting) took place on December 7, 1987, the second on February 9, 1988 yet there was no discussion/ agreement at the Board level as to what operational costs NEL was to be responsible for nor how these operational costs were to be determined.

It is to be noted that by correspondence dated February 16, 1988 to the Board of Directors of NEL, P.D. Sprung in his role as contractor forwarded documentation supporting charges of $300,687.59 paid by Sprung Environmental Space Enclosures Limited (SESE) on behalf of NEL.

C.D. 007, pp. 029-031

It is further noted that a cheque dated February 17, 1988 made payable to SESE by NEL for $300,687.59 was deposited in a SESE account February 18, 1988 prior to the matter being dealt with by the Board of Directors of NEL on February 19, 1988.

C.D. 007, p. 032

The Cost Summary as presented to the Board of NEL on February 19, 1988 was accepted

> "subject to further discussion and review respecting NEL's takeover of production and liability for costs prior to the initial planting".

There was no further discussion and review of the matter at the Board level.

The cost summary presented to the Board on February 19, 1988 was:

SUMMARY OF COSTS PAID BY SPRUNG ENVIRONMENTAL SPACE ENCLOSURES LTD. ON BEHALF OF NEWFOUNDLAND ENVIROPONICS LTD.

1. SEED PLANTING AND NUTRIENTS	
Van Waters - Nutrients	$ 9,232.00
Prairie Industrial - Nutrients	736.33
Canadian - Freight	125.44
Day and Ross - Freight	147.55
Seed Company - Back pack Sprayers	102.94
A & K Petro Chem-Nutrients	3,561.00
2. HEAT LIGHT AND POWER	
C. L. A. - CO2	106.25
Superior - Propane	179.20
	311.95
	424.18
	274.35
	2,205.21
	2,201.13
	2,965.01
	2,895.20
	2,287.46
	1,636.59
3. PRODUCTION SALARIES TO FEB. 6TH	58,141.36
Supervisors	7,442.08
4. MANAGEMENT TO FEB. 6TH P. 1032 P. 1033-35	11,686.88
5. LABORATORY	
Memorial University - Testing	25.69

6. MAINTENANCE

Kent - Training	2,812.53
Canadian Tire - Shop Vac	180.49
Honda One - Snow Blowers	3,942.40
Tors Cove - Snow Removal	457.50

7. ELECTRICAL

Prince - Labour	8,167.25
Capital Crane - Move equipment	2,600.00
Atlantic - Concrete Pads P 1043	5,000.00
N L & P - Stress Cones 1043	1,250.00
Carpenters - Material Labour & covers	4,000.00
Union Electric - Copper Rods	495.94
Wesco - Switch gear Fittings	3,876.49
Keough - Terminating H.V. Cables	1,700.00
Keough - Terminating H.V. Cables	600.00
Wesco - Conductor 1000 MCM MV90	6,582.00
Wesco - Switch Gear	66,690.00
Wesco - Conduit	300.00
Wesco - PVC	35.30
Wesco - PVC	34.30
Wesco - 15 KV Shield	22,114.00
Tors Cove - lay out cable labour	423.00
Tors Cove - lay out cable equipment	6,850.00
Tors Cove - Rock for H.V. Trench	1,020.00
Tors Cove - Sand for H.V. Trench	3,069.33
Heap Noseworthy - Electrical Strap	21.31
Annixter - Connectors	404.79
NL&P - Supply and install 12500 V line	7,500.00
Union Electric - Conduit	300.74
Union Electric - Straps	32.00
Union Electric - Electrical Supplies	651.63
Union Electric - Conduit	1,023.00
Cassie - Engineering	3,261.44
Cassie - Engineering	2,775.00
Cassie - Engineering	4,267.50
Ian McKay - Engineering	3,333.00
Annixter - Teck "90 1KV	2,356.70
Annixter - Copper Stranded	688.63
Harris & Roome - Breaker boxes	7,406.25
Ted Cap - Generator Rental	1,800.00

8. ADVERTISING	
Globe and Mail - Advertising for Plant Physiologist	833.80
Grower Magazine - Magazine	54.68
Agriculture Canada - License	500.00
9. MANAGEMENT TO CLERICAL	5,067.64
10. OFFICE AND ACCOUNTING	
D.N.A. - N.E.L. Software	7,025.60
Daca Best - N.E.L. Letterhead	487.20
Daca Best - Rent P 1043	1,200.00
TOTAL	**$300,687.59**

The Summary of Costs covered an array of items presumably covering the operational costs of SESE the contractor relating to the maintenance of plants after the first initiation (planting) and up to February 6, 1988 and included in that regard, seed, nutrients, heat, production salaries, etc.

The Summary of Costs also included Electrical costs that presumably related to the growing lights.

C.D. 007, pp. 002-003

If Sprung was not to be responsible for the costs of the growing lights as suggested, were the electrical charges in the Summary of Costs pertaining to the growing lights?

The following items as listed in the said Summary of Costs may not have pertained to the growing lights:

Prince - Labour	$ 8,167.25
Union Electric - Copper Rods	495.94
Wesco - Surtek Gear Fittings	3,876.49
Wesco - Conduit	300.00
Wesco - PVC	35.30
Wesco - PVC	34.30
Heap Noseworthy - Electrical Strap	21.31
Annixter - Connectors	404.79
Union Electric - Conduit	300.74
Union Electric - Straps	32.00
Union Electric - Electrical Supplies	651.63
Union Electric - Conduit	1,023.00
Annixter - Teck "90 1KV	2,356.70
Annixter - Copper Stranded	688.63

Harris & Roome - Breaker Boxes	7,406.25
Ted Cap - Generator Rental	1,800.00
TOTAL	**$27,594.63**

The following items as listed in the said Summary of Costs could have related to the growing lights but not exclusively and an allowance in favour of NEL should therefore have been made in that regard:

NL&P - Stress Cones - $1,250.00 **Allowance in Favour of NEL**

When installation on high voltage cable is cut, stress cones cover the ends. Each end of a cable would have a stress cone. NL&P put in main stress cones to the main switch gear giving power to the site. The majority of the power load to site was for the growing lights but the load also gave power to pumps and other electrical requirements. The percent of the load required for the growing lights 7.4 mega volt amps is 85-87%. The growing lights required 87% of the load to the site.

13% of $1,250 not required for growing lights. $ 162.50

Keough - Terminating H.V. Cables - $1,700.00
Keough - Terminating H.V. Cables - 600.00

Terminating H.V. Cables means putting stress cones on cables. There were 6 cables (loads) to site, 5 were related to providing power for lights.

1/6 or 16.66% of $2,300 not related to growing lights. $ 383.18

Wesco - Conductor 1000 MCM MV90 - $6,582.00

Relates to the cable coming from the pole to the main switch gear to supply power to the site. The demand load for the growing lights was 87%.

13% of $6,582 not related to growing lights. $ 855.66

Wesco - Switch Gear - $66,690.00

This switch gear would not be required if there were no growing lights. In absence of growing lights to bring power to site what is required is a pole mounted disconnect bringing load from a pole to Sprung's Transformer. The cost of providing power without the switch gear would be in the $2-$3,000 range. $ 2,500.00

Wesco - 15 KV Shield - $22,114.00

This relates to high voltage cable from the main switch gear to 5 transformers. The total length of 15KV cable not related to the growing lights would be in the 20-25% range of 15KV cable on site.

25% of $22,114.00 not related to growing lights. $ 5,528.50

Tors Cove - Lay out Cable Labour	**$ 423.00**
Lay out Cable Equip.	**6,850.00**
Rock for H.V. Trench	**1,020.00**
Sand for H.V. Trench	**3,069.33**

Relates to the laying of the 15KV shield in Trench.

25% of $11,362.33 not related to growing lights. $ 2,840.58

NL&P - Supply & Install 12500V line $7,500.00

This was the main line bringing power to the site. In the absence of growing lights, one would not require such a line. The line also supplied power elsewhere to the site. The cost of putting in 12500V line (3 Cables) was $7,500.00. The 3 phase line installed was of a greater capacity than the 3 phase line which would have been installed if the growing lights were not required. A reasonable estimate for the latter. $ 5,500.00

C.D. 007, pp. 050-057

TOTAL **$17,770.42**

Findings:

- **that the Company assumed the responsibility for the Sylvania Lighting System and took on the obligation to pay the debenture owing to Sylvania in the amount of $3,400,000 which was to be retired in quarterly instalments over seven years.**

- **that only three payments were made on the debenture totalling $552,400 during the period March 21, 1988 through February 15, 1989.**

- **that the owner (NEL) paid the contractor (SESE) the sum of $300,687.59 by cheque dated February 17, 1988 which cheque was deposited in a SESE account on February 18, 1988 prior to the matter of the reimbursement of SESE by NEL being dealt with at a Board of Directors Meeting of NEL on February 19, 1988.**

- **that there was no proper and effective monitoring by Government to confirm the appropriateness of the electrical charges submitted by the contractor Sprung to NEL for reimbursement as there should have been.**

- **that the sum of $27,594.13 paid by NEL to SESE for electrical charges may not have pertained to the growing lights.**

- **that the sum of $17,770.42 paid by NEL to SESE may not have related exclusively to the growing lights.**

QUESTIONABLE ITEMS IN THE SUMMARY OF COSTS PURPORTEDLY RELATING TO GROWING LIGHTS.

(1). Cassie Engineering

C.D. 007, p. 033	(a) invoice dated Sept. 25, 1986	**$3,261.44**
C.D. 007, p. 034	(b) invoice dated Aug. 31, 1987	**$2,775.00**
C.D. 007, p. 035	(c) invoice dated Nov. 04, 1987	**$4,267.50**

It is further noted that by a Board of Directors meeting of NEL held on the 18 day of May 1988 on the Chairman Mr. P.D. Sprung's recommendation, it was resolved that:

C.D. 007, p. 036-046

> "the Company (NEL) retain G. Cassie of Calgary as a consultant to advise in all aspects of the lighting system design and remedial work".

It is further noted Delta Electric was the subcontractor for the installation of the growing lights and the BAE Group consultants for the installation and for review of and redesign of lighting plans. It appears Cassie Engineering had an involvement with the growing lights in 1988 and not in 1987.

C.D. 007, p. 004
C.D. 007, pp. 047-049
C.D. 007, pp. 050-057

Findings:

- **that there is insufficient documentation and information relating to Cassie Engineerings' above noted invoices, to determine why in fact NEL should have reimbursed the contractor (Sprung) for said invoices as it appears the said invoices may not have been properly related to the growing lights.**

- **that Government was remiss in not confirming the appropriateness or otherwise of the said invoices.**

(2). Ian Mckay

(a) Engineering Services **$3,333.00**

Mr. Mckay's main responsibility was in the area of production. He did have a very minor involvement with the growing lights, providing access to production zones for lighting personnel and maintaining the monitoring of the lights.

C.D. 007, pp. 050-057

Findings:

- **that insufficient documentation exists to determine the extent of Mr. McKays involvement as it related to the growing lights and why in fact NEL should have reimbursed the contractor (Sprung) for the said amount as it appears McKays involvement was minor to say the least.**

- **that Government was remiss in not confirming the appropriateness or otherwise of the said invoice.**

(3). Salaries to February 6, 1988

(a) Production Salaries	**$58,141.36**
(b) Supervisors Salaries	**7,442.08**
(c) Management Salaries	**11,686.88**

Finding:

- **that the determination of production, supervisor, and management salaries were entirely within the domain of the contractor (SESE) who made the allocation. There was no monitoring by Government to confirm the appropriateness or otherwise of the salaries as presented. This pertains to subsequent payroll invoices paid by NEL from March - June of 1988 for operating expenses after the first initiation and prior to turn over.**

SUBSEQUENT INVOICES TO NEL FOR REIMBURSEMENT OF OPERATING EXPENSES PAID BY CONTRACTOR (SPRUNG) WERE:

March 21, 1988	Expenses	**$ 40,706.23**
March 21, 1988	Payroll	**39,218.63**
March 25, 1988	Payroll (Mar 6-19)	**21,335.44**
April 15, 1988	Payroll (to Apr. 2)	**47,614.05**
May 4, 1988	Payroll (to Apr. 15)	**52,171.54**
May 12, 1988	Payroll (to Apr. 30)	**79,306.54**
June 6, 1988	Payroll (to May 14)	**89,426.27**
June 6, 1988	Expenses	**14,255.84**
June 10, 1988	Payroll (to June 11)	**124,661.49**
June 15, 1988	Payroll (to May 28)	**121,306.84**
June 22, 1988	Expenses	**87,942.83**

C.D. 015, pp. 001-130

Findings:

- that there were certain questionable operating expenses paid by NEL to SESE on the invoices of March 21, 1988 June 22, 1988.

    - on the invoice of March 21, 1988, there were charges for apartment rental of $2,350.00 and employee relocation costs of $630.00.

    - on the invoice of June 22, 1988, there were charges for security of $2,331.00, computer rental from an employee of $2,300.00 and flowers to employees of $44.00 and $48.50 respectfully.

- that Government was utterly remiss in failing to monitor and confirm the appropriateness or otherwise of the charges relating to production supervisor and managment salaries to February 6, 1988 and invoice charges subsequent to March 21, 1988 all of which were paid by NEL to SESE, it appears without question.

- that the total amount of operating costs invoiced to NEL for reimbursement to SESE and paid to SESE was $1,020,002.

Invoices paid directly by NEL for Operating Expenses in relation to initiating and subsequent maintenance (operations) were:

DATE	INVOICE DESCRIPTION	SUPPLIER	AMOUNT
Jan. 4/89	Water Filters	Basil Fern	$ 358.40
Jan. 29/88	CO2	Canadian Liquid Air	179.22
Jan. 29/88	CO2	Canadian Liquid Air	537.66
Jan. 29/88	CO2	Canadian Liquid Air	548.19
Jan. 29/88	CO2	Canadian Liquid Air	179.22
Feb. 12/88	CO2	Canadian Liquid Air	358.44
Feb. 5/88	C02	Canadian Liquid Air	537.66
Feb. 17/88	CO2	Canadian Liquid Air	358.44
Jan. 14/88	CO2	Canadian Liquid Air	94.87
Feb. 10/88	CO2	Canadian Liquid Air	906.63
Jan. 29/88	CO2 Manifold	Canadian Liquid Air	84.70
Jan 29./88	Hoses/Connectors	Canadian Liquid Air	21.83
Feb. 19/88	Hydrogen, CO2	Canadian Liquid Air	314.15
Feb. 23/88	Nitrogen Regulators	Canadian Liquid Air	238.14
Feb. 24/88	H2O Jug, Tea Towels (Wrapping)	Canadian Tire	29.89

DATE	INVOICE DESCRIPTION	SUPPLIER	AMOUNT
Feb. 19/88	Laundry Baskets (Selection)	Canadian Tire	89.85
Feb. 19/88	Laundry Baskets (Selection)	Canadian Tire	59.90
Mar. 2/88	Power Bar (Wrapping Machines)	Canadian Tire	19.99
Mar. 3/88	Rubber Gloves	Canadian Tire	17.88
Mar. 9/88	Scissors (Selection)	Canadian Tire	31.96
Jan. 29/88	Lumber (Switch gear)	Chester Dawe	130.89
Feb. 19/88	Copy Paper	Dacabest Printing	50.00
Feb. 19/88	NEL Invoice Books	Dacabest Printing	713.70
Jan. 15/88	Caustic Soda	East-Chem	28.30
Jan. 29/88	Phosphoric Acid	East-Chem	68.30
Mar. 10/88	Misting Kit	Gaze Seed Co.	30.48
Feb. 19/88	Snowblower Repair	Honda One	25.04
Feb. 29/88	Hard Hats	J.C. Pratt	99.75
Feb. 2/88	Gas Detector	Kerr Controls	68.58
Feb. 16/88	Coverall Cleaning	Laundromat, The	27.30
Jan. 29/88	Brass Numbers	M.A. Parsons	17.97
Feb. 16/88	Cucumber Boxes	Nfld. Containers	3,965.95
Jan. 21/88	Lettuce Boxes	Nfld. Containers	2,218.25
Jan. 28/88	Tissue Analysis	Norwest Labs	134.00
Jan. 25/88	Tissue Analysis	Norwest Labs	171.00

DATE	INVOICE DESCRIPTION	SUPPLIER	AMOUNT
No Date	Shoes	Parker & Monroe	234.00
Mar. 8/88	Computer Supplies	Radio Shack	27.95
Feb. 11/88	Digital Scale	Scale Shop	150.58
Mar. 1/88	Propane	Superior	454.37
Feb. 16/88	Propane	Superior	19,443.97
Feb. 15/88	Propane (Admin)	Superior	431.73
Dec. 8/88	Propane (Admin)	Superior	181.65
Feb. 3/88	Coverall Cleaning	Top Tone	17.55
No Date	Coverall Purchases	Top Tone	2,437.50
	Coverall Purchases	Top Tone	1,462.50
Feb. 19/88	Repair to Glass Partion - Admin	Tulks	127.80
Feb. 4/88	Transformer	Wesco	16,500.00
		TOTAL:	**$54,186.13**

The amount of invoices paid directly by NEL for operating costs subsequent to initiation minus the electrical charges amounted to $54,186.13.

It further appears the invoice of $16,500 from Wesco dated February 4, 1988 for a transformer should not have been paid by NEL but was the responsibility of the Contractor Sprung.

C.D. 007, pp. 050-057

Findings:

- **that with reference to the above noted invoices, it is noted by invoice dated February 04, 1988 from Wesco to NEL Re: transformer in the amount of $16,500.00, did not, it appears pertain to the growing lights and should therefore have been the responsibility** of the contractor (Sprung) and should not have therefore been paid by the owner (NEL).

- that the total cost pertaining to the major changes to the Construction Agreement and Shareholders Agreement was $1,074,188.13 (1,020,002.00 + 54,186.13).

- that the changes to the (C.A.) and (S.A.), involving such a large sum of money should have been clearly defined and documented setting forth the obligations/responsibilities of the contractor and owner and how each obligation and responsibility was to be determined.

- that there was no proper and effective monitoring by Government to confirm the appropriateness or otherwise of the reimbursement by NEL to SESE in the amount of $1,020,002.00 nor of the invoices paid by NEL in the amount of $54,186.13.

- that the noted changes to the Construction agreement and Shareholders Agreement should have been approved by the Board of Directors of NEL. Article 7.1 (ix) Shareholders Agreement required the consent of Government for "any transactions between the Company and Sprung other than those specifically permitted by this Agreement". The changes to the Construction Agreement and Shareholders Agreement were not provided for in either Agreement. Government did not give its consent to the changes to the Shareholders agreement (and therefore the Construction Agreement) as required by Article 7.1 (ix) of the Shareholders Agreement.

PART VIII

ELECTRICITY (ENERGY) PROVISIONS SHAREHOLDERS AGREEMENT

Article 9.1 of the Shareholders Agreement provided that:

> "Sprung shall be liable for the payment of the cost of all electricity consumed at the Facility (other than that consumed by the Lights) in excess of 26.5 million kilowatt hours (net) per year".

Article 9.2 of the Shareholders Agreement provided that:

> "for any year in which the electricity consumed at the Facility (other than electricity consumed in operating the Lights) is less than 26.5 million kilowatt hours (net) Sprung shall receive a payment from the company equal to the amount by which the cost of 26.5 million kilowatt hours (net) exceeds the cost of such electricity actually consumed at the Facility".

C.D. 001, p. 048

The calculations of payments under Article 9.1, 9.2 of the Shareholders Agreement was by a formula set forth in Articles 9.3, 9.4 of the Shareholders Agreement.

C.D. 001, p. 049

Article 9.5 of the Shareholders Agreement provided that:

> "the Company (NEL) shall maintain records of operations satisfactory to the Government and Sprung necessary to make the calculations required by paragraph 9.3 and shall make the records available on request for audit by the Company's auditors".

Article 9.6 of the Shareholders Agreement provided that:

> "if a form of energy other than electricity is used at the Facility, this Article shall still apply and all references to electricity shall be deemed to be references to the equivalent energy usage of the form of energy actually used".

C.D. 001, pp. 049-050

Article 10.3 of the Shareholders Agreement provided that:

> "Sprung shall be liable for payment of the cost of all electricity consumed at the Facility for the operation of the Lights".

Article 10.4 of the Shareholders Agreement provided that:

> "Sprung shall ensure that meters are installed at the Facility to permit the measurement of electricity consumed in operating the Lights separate from the measurement of other electricity consumed at the Facility".

Article 10.5 of the Shareholders Agreement provided that Sprung would be reimbursed for lighting costs according to a formula set forth therein.

C.D. 001, p. 051

(M/C 1048-'88) dated July 14, 1988 states:

> "ordered that Government defer enforcement of the energy provisions of the Shareholders Agreement between the Province and the Sprung Group of Companies pending an accounting at year end to allow Newfoundland Enviroponics Limited to operate as if energy costs were the same as any other operating cost of the Company, with Mr. Sprung to be advised accordingly".

C.D. 002, p. 037

As a result of the deferred enforcement of the energy provisions of the Shareholders Agreement Sprung was effectively relieved of his obligations to pay the energy costs as set forth in the Energy provisions of the Shareholders Agreement at least until the end of 1988 at which time an accounting would be undertaken to determine the energy costs associated with NEL. Energy costs as a result of the deferment were to become an operating cost of NEL.

By Article 10.4 of the Shareholders Agreement Sprung was to install meters to permit the measurement of electricity consumed in operating the lights separate from other electricity consumed at the Facility.

C.D 001, p. 051

It is noted at a Board of Directors meeting of NEL held on February 10, 1988 the Chairman of the Board Mr. Philip Sprung advised in response to an inquiry from a government appointed director that separate electricity meters for the lights had not been installed to date but were on order.

C.D. 003, pp. 022-026

Findings:

- **that if the Company did maintain records of operations pursuant to Article 9.5 of the Shareholders Agreement, the said records were not maintained at the Facility where they should have been. No known records exist to make the calculations required by Article 9.3 of the Shareholders Agreement.**

- **that Government did not provide for an accounting at either the fiscal year end of NEL on November 30, 1988 nor at the end of the calendar year 1988 to determine the energy costs of the operation pursuant to the Shareholders Agreement nor did Government determine at years end if Sprung's obligations under the energy provisions of the Shareholders Agreement would cease or remain in full force and effect.**

- **that no meter/s to permit the measurement of electricity consumed in operation of the lights were installed as they should have been.**

- **that it was incumbent upon Government to ensure at the earliest opportunity the installation of meter/s to permit the measurement of electricity consumed in operation of the growing lights for which Sprung pursuant to the Shareholders Agreement was liable and which was pertinent to the overall energy provisions (costs) of the Shareholders Agreement.**

A CALCULATION OF ENERGY COSTS FOR 1988 PURSUANT TO PROVISIONS OF THE SHAREHOLDERS AGREEMENT

The total (kwh) of electrical energy supplied to the site in 1988 was 22,701,492 (kwh).

The percentage of that total used for the growing lights has been determined to be 85% or 19,296,268 (kwh).

C.D. 008, pp. 001-005

The electrical energy supplied for other than the growing lights then is 3,405,224 (kwh).

C.D. 008, pp. 006-014

The total propane supplied to the site in 1988 was 845,470 litres.

By virtue of Article 9.6 (S.A.)

C.D. 001, p. 050

> "if a form of energy other than electricity is used all references to electricity (in the electricity provisions of the Shareholders Agreement) shall be deemed to be references to the equivalent energy usage of the form of energy actually used."

845,470 litres of propane is then converted to 4,495,787 (kwh) assuming the furnaces are operating at 75% efficiency.

The total energy consumption for 1988 other than for the growing lights is then:

(kwh) consumed other than for growing lights	3,405,224
Propane converted to (kwh)	4,495,787
Total (kwh) other than for growing lights	**7,901,011**

The lowest cost/kwh in 1988 was:

C.D. 012, pp. 114-129

- $0.05426 on the first 100,000 kwh/month
- $0.03996 on the balance or excess over 100,000kwh/month

ASSUMPTIONS IN DETERMINING COST:

(a). for purpose of Articles 9.3 and 9.4 of the Shareholder's Agreement, it is assumed there were no "Shutdown days".

(b). The reference to "electricity consumed" in Articles 9.1, 9.2 of the Shareholders Agreement implies "demand charge".

IN CALCULATING THE TOTAL (KWH) USED FOR THE GROWING LIGHTS IN 1988 AT COST PER (KWH) THE FOLLOWING CALCULATIONS APPLY.

The total (kwh) used for the growing lights in 1988 of 19,296,268 minus the cost/kwh in excess of 100,000 kwh/month multiplied by the cost/kwh of $0.03996 is $723,126.86.

The cost of (kwh) in excess of 100,000 (kwh)/month is (12 X 100,000) multiplied by 0.05426/kwh which is $65,112.00.

The total cost ($723,126.86 + $65,112.00) is $788,112.00.

The demand charge must be included as a cost factor.

The demand charges from January 1 - December 1988 total 77,977 kilovoltampere.

The average cost kilovoltampere is determined at $5.00.

The cost of 77,977 kilovoltampere at $5.00/kilovoltampere is 389,885.

85 % of the total cost of the kilovoltampere of 389,885 related to the growing lights is $331,402.

The total cost of electricity for the growing lights in 1988 is calculated to be (788,112.00 + 331,402) $1,119,514 and was the responsibility of Sprung pursuant to Article 10.3 of the Shareholders Agreement.

In calculating the electricity costs pursuant to Articles 9.1, 9.2 of the Shareholders Agreement it is noted that Sprung was to be liable for the cost of all electricity consumed in excess of 26.5 m kwh net/year, and for any year in which the electricity consumed (other than for growing lights) was less than 26.5 m kwh net/yr. Sprung was to receive a payment from the Company (NEL) equal to the amount by which the cost of 26,500,000 kwh net/yr exceeded the cost of such electricity actually consumed.

The total energy consumed by virtue of Article 9.2 Shareholders Agreement is as follows:

Total energy consumed other than for growing lights as determined is 7,901,011 (kwh).

Pursuant to Article 9.2 the difference (26.5 m and 7,901,011 kwh) of 18,598,989 (kwh) is the credit due Sprung.

To determine the cost of the 18,598,989 (kwh) the following calculations apply:

18,598,989 (kwh) minus the cost/(kwh) in excess of 100,000 kwh/month, multiplied by the cost/kwh of $0.03996 is 695,264.

The cost of (kwhs) in excess of 100,000 (kwh)/month is (12 X 100,000) X 0.05426 is 65,112.

To apply a proportionate demand charge, the following calculations are used:

$\frac{18,598,989}{19,296,268}$ X 77,977 = 75,154 X $5/KVA for a demand charge of (375,772 X 85%) 319,406.

Total cost and payment due Sprung pursuant to Article 9.2 Shareholders Agreement is (695,264 + 65,112 + 319,406) 1,079,782.

An alternative method of calculation is to divide the Sprung credit of (18,598,989 KWA) by the total consumption of (22,701,422 KWA) multiplied by the total billings for that period of ($1,292,827). This amount would then be subtracted from 85% of the total billings of ($1,098,903).

$\frac{\$18,598,989}{\$22,701,492}$ X $1,292,827 =	**$1,059,194**
$1,098,903 - $1,059,194 =	**$ 39,709**
Sprungs Apparent Liability -	**$ 39,709**

Finding:

- **that had there been no deferment of the energy provisions, based on the above energy calculations, it would appear Sprung was liable for $39,838 ($1,119,620 - $1,079,782) in energy costs for the calendar year 1988.**

PART IX

COMMENTS: SHAREHOLDERS AND CONSTRUCTION AGREEMENTS

Article 4.2 of the Shareholders Agreement specifies:

> "Government shall transfer the sum of $3,500,000 to the company", (Newfoundland Enviroponics Limited).

C.D. 001, p. 035

Article 4.4(a) of the Shareholders Agreement specifies Sprung shall:

> "advance by way of loan to the company $3,500,000 as evidenced by a Promissory Note in the form annexed as Schedule "A".

C.D. 001, p. 035

A Promissory note was in fact executed by NEL on December 10, 1987 for the stipulated amount. The note was due and payable by instalments however the amount of the instalments as a percent (%) of the company's yearly net profits was not set forth in the said promissory note as it should have been.

C.D. 003, pp. 001-002

Article 4.8 of the Shareholders Agreement specifies the transfer or advance by Government and Sprung of each $3,500,000 in equity was to be made as follows:

> (a) $1,500,000 on the date specified in Section 4.2 (iii) of the Construction Contract and
>
> (b) On each subsequent payment date as specified in section 4.2(iv) of the Construction Contract an amount equal to one-half of the payment so specified on that date until the total payments made by Government and Sprung shall each equal $3,500,000.

C.D. 001, p. 037

By (MC 1131-87) dated September 29, 1987 government authorized an amendment to the Construction Contract and approved its execution by Newfoundland Enviroponics Limited.

C.D. 003, p. 003

It is noted the amendment to the Construction Agreement is dated September 24, 1987 and duly executed and witnessed by the parties thereto.

C.D. 001, pp. 110-113

The amendment related to the payment schedule of the contract price with particular reference to paragraphs 4.2(iii), (iv) of the Construction Contract.

Prior to the amendment, paragraphs 4.2(iii), (iv) of the Construction Contract read:

iii) $4,000,000 following:

  (a) receipt of plans and designs for completion of the work duly stamped by a qualified engineer entitled to practice in Newfoundland, and

  (b) arrival of the Existing Facility and Equipment from Calgary.

iv) $6,325,000 by instalments in accordance with a payment schedule to be agreed upon following receipt of the said plans and designs referred to in sub-paragraph (iii) and to be based upon completion of specified portions of the Work. Failing agreement, the payment schedule shall be settled by arbitration pursuant to Article XI.

C.D. 001, p. 086

The amendment deleted paragraphs 4.2 (iii), (iv) of the Construction Contract and substituted the following:

iii) up to $1,000,000 following delivery to the owner's Lands of a substantial portion of the Existing Facility and Equipment.

iv) $4,000,000 less any amounts paid pursuant to paragraph (iii) following:

  (a) receipt of plans and designs for completion of the work duly stamped by a qualified engineer entitled to practice in Newfoundland, and

  (b) delivery and acceptance of the remaining portion of the Existing Facility and Equipment to the Owner's Lands.

> v) $6,325,000 by instalments in accordance with a payment schedule to be agreed upon following receipt of the said plans and designs referred to in sub-paragraph (iv) and to be based upon completion of specified portions of the work. Failing Agreement, the payment schedule shall be settled by arbitration pursuant to Article XI.

C.D. 001, pp. 111-112

It is to be noted the Construction Contract in particular was a self financing document in favour of the Contractor such that Sprung's advance by way of loan to the Company of $3,500,000 to be evidenced by a promissory note pursuant to Article 4.4(a) of the Shareholders Agreement was intended to be deducted from the stipulated contract price of $14,325,000.

C.D. 003, p. 009

It is to be noted further that pursuant to Article 4.4 (c) of the Shareholders Agreement Sprung was to provide a guarantee to a lending institution, on terms and conditions satisfactory to the Shareholders (of Newfoundland Enviroponics Limited) for a $500,000 loan to be obtained by the Company for construction of the Facility.

C.D. 001, p. 035

It is also to be noted that the Contractor (Sprung) was paid $4,000,000 on November 19, 1987 pursuant to the Statutory Declaration of Philip Sprung dated November 19, 1987 and made pursuant to section 4.2 of the Construction Contract for payment of monies upon delivery and acceptance of the Existing Facility and Equipment.

C.D. 003, pp. 007-008

It is further noted that $1,500,000 of Sprung equity of $3,500,000 was on November 19, 1987 credited towards Sprungs equity account pursuant to Article 4.8 (a) Shareholders Agreement.

C.D. 003, p. 009

Findings:

- **that not only was the Construction Contract amended without proper Government authority, the amendment to the Construction Contract rendered inoperable Article 4.8(a) of the Shareholders Agreement since by virtue of the amendment only $1,000,000 was now to be advanced to the contractor (Sprung) by virtue**

of Article 4.2 (iii). In other words, Sprung would have to finance the additional $500,000 to honour his commitment pursuant to Article 4.8(a) of the Shareholders Agreement to make the first advance or instalment in his equity contribution of $1,500,000. This was obviously not the intent of the Construction Contract.

- **that the payment of $4,000,000 to Sprung was not in accordance with the amendment to Article 4.2 (iii) of the Construction Contract but purported to be paid pursuant to Article 4.2 (iii) Construction Contract prior to its amendment.**

- **that the amendment to the Construction Contract was it appears not acted upon and was not rescinded.**

- **that the $4,000,000 payment to Sprung was not in accordance with Article 4.2 (iii) of the Construction Contract prior to its amendment. Article 4.2(iii) provided payment, upon plans and designs for completion of the work being duly stamped as therein indicated and arrival of all of the Existing Facility and Equipment from Calgary.**

- **that Philip Sprung's affidavit of November 19, 1987 indicated in excess of 98% of the Existing Facility and Equipment had been delivered and accepted on site. Common practice should have dictated a holdback by Government until the remaining equipments arrival was confirmed. There was no confirmation of the arrival of the approximately 2% of the remaining Facility and Equipment worth allegedly some $80,000.**

CONTRACT PRICE

C.D. 001, p. 076

By Article 1.1(g) of the Construction Contract price means "the sum of $14,325,000".

C.D. 001, pp. 085-086

Article 4.2 Construction Contract regarding payment schedule provides for a total payment of "$14,425,000 to the contractor", a $100,000 discrepancy over and above the contract price as defined.

Finding:

- **that while the Construction Contract was never formally amended to reflect the true contract price, the $100,000 discrepancy was recognized and not paid to the contractor Sprung.**

CLASS B SHARES (S.A.)

It is to be further noted with regard to Article 4.5 (a) of the Shareholders Agreement that the Company (Newfoundland Enviroponics Limited) would issue out of treasury to Government in consideration of matters specified in paragraph 4.2 (a) and (b) of the Shareholders Agreement 3500 Class B shares as fully paid and nonassessable.

C.D. 001, p. 036

Article 4.2 Shareholders Agreement contains no paragraphs (a) and/or (b).

It is noted 3500 Class B Shares were issued to Government (NIDC).

C.D. 001, pp. 123-124

Finding:

- **that it is reasonable to conclude that the reference to paragraphs 4.2 (a) and (b) in Article 4.5 (a) of the Shareholders Agreement refers to Article 4.2 and that 3500 Class B shares were issued to Government in consideration of governments equity of $3,500,000.**

REMUNERATION OF SENIOR MANAGEMENT (S.A.)

By Article 7.1(ii) of the Shareholder's Agreement, the consent of Government was required for the determination of the remuneration and benefits for management employees of Newfoundland Enviroponics Limited, including a profit sharing plan.

Article 7.1 of the Shareholders Agreement reads:

> Sprung will be responsible for management of the Company subject to the consent of the Government, (which consent shall not unreasonably be withheld) with respect to the following:
>
> i) any capital expenditure of the company exceeding $100,000 per annum;
>
> ii) remuneration and benefits for management employees of the Company, including a profit sharing plan;
>
> iii) the authorized and issued capital of the Company and any subsequent changes thereto except as permitted by this Agreement;
>
> iv) the declaration and payment of dividends on issued Shares of the Company;
>
> v) the appointment of the Chief Executive Officer and other officers of the Company;
>
> vi) the provisions contained in the articles and by-laws of the Company and any subsequent amendments thereto;
>
> vii) the wind-up, liquidation or dissolution of the Company;
>
> viii) the original and subsequent business plans of the Company and any amendments thereto;
>
> ix) any transactions between the company and Sprung other than those specifically permitted by this Agreement;
>
> x) fees and expenses payroll to Directors of the Company;
>
> xi) borrowings by the Company in excess of $100,000 per annum;
>
> xii) the appointment of the auditors and legal counsel of the Company;
>
> xiii) hiring of consultants by the Company for any purpose; and
>
> xiv) the selection by the Company of the Owner's Representative under the Construction Contract;

xv) such other matters as may be agreed by Sprung and the Government.

C.D. 001, pp. 042-043

Article 10.7 of the Shareholders Agreement provided that:

> "it is recognized that for purposes of the Cash Flow Projection attached to this Agreement as Schedule "B", the following items are not finalized and Sprung and Government agree that this Schedule will be amended to reflect the actual status of the following items":

i) Eligibility under the Provincial Job Creation Program

ii) Long term debt - principal and interest

iii) Leasing principal and interests

iv) Municipal taxes

v) Consulting

vi) Investment Tax Credits

vii) Research and Development Tax Credits

viii) Federal and Provincial Income Tax

xi) Energy Costs

x) Working Capital Interest

C.D. 001, p. 053

By (MC 1048-'88) dated July 14, 1988 government approved the remuneration of Mr. Philip Sprung, Chief Executive Officer of Newfoundland Enviroponics Limited and other senior management employees. Salaries ranged from $20,000 for production employees to $71,711/annum for the Chief Executive Officer. No other remuneration and or benefits (fringe or otherwise) pertaining to senior management employees were approved by Government.

C.D. 002, pp. 037-038

At a Board of Directors Meeting of Newfoundland Enviroponics Limited held on the 19th day of February 1988, there was a discussion respecting the allocation of moving costs of operational and construction personnel. Nothing appears to have been resolved by the Board of Directors regarding such moving costs.

C.D. 003, pp. 010-016

Senior Management employees of NEL did receive benefits other than remuneration not approved by Government nor by the Board of Directors of NEL.

Newfoundland Enviroponics Limited paid the:

1). Rent for two senior management employees	
(a) one - June 1988-March 1988	**$5,200.00**
(b) two - October 1988-March 1989	**$2,500.00**
2). Airfare St. John's to Calgary return once a month for two senior employees.	
(a) one - June 1988-December 1988	**$8,487.00**
spouse - July 1988	**$ 705.00**
(b) two - May 1988-December 1988	**$5,256.35**
3). Paid the airfare once/year for a trip home for employees who resided out of the province, this pertained to some 10 employees with airfare of	**$8,205.01**
4). Paid relocation costs for at least three employees amounting to	**$3,860.94**

C.D. 003, pp. 017-020

Findings:

- **that payment of the above noted benefits was in breach of Article 7.1(ii) of the Shareholders Agreement since Government nor the Board of Directors of NEL consented to the payment of such benefits.**

- **that the consent of Government pursuant to Article 7.1 of the Shareholders Agreement was required with respect to all the enumerated items therein.**

- **that Schedule B to the Shareholders Agreement was never amended to reflect the actual status of items (i) - (X) as set forth in Article 10.7.**

COMPLETION DATE (C.C.)

Article 2.2 of the Construction Contract provides:

C.D. 001, p. 081

> The contractor shall effect completion of the work on or before the completion date.

Article 1.1(f) of the Construction Contract defines completion date as:

C.D. 001, p. 076

> the period of 180 days from the date by which this Agreement (Construction Agreement) is executed by the owner and delivered to the contractor, subject to extensions as permitted in Article VI (delays beyond the control of the contractor) and Article VII (site changes not anticipated, regulatory and owner's changes).

Article 1.1(y) Construction Contract defines work as:

C.D. 001, p. 078

> the commencement, prosecution and completion of construction of the Production Facility in accordance with the specifications and includes the installation of the Equipment and preparation for start-up as set forth in Section 8.6.

C.D. 003, p. 021

The completion date would in effect therefore be on or about December 25, 1987. It is noted on December 21, 1987 the contractor requested a 90 day extension to the contract.

C.D. 003, pp. 022-026

It is further noted that at a Board of Directors meeting of Newfoundland Enviroponics Limited held on February 10, 1988 the secretary was directed to prepare and submit at the next Board Meeting an amendment to the Construction Agreement extending the completion date to April 30, 1988.

Finding:

- **that no formal amendment to the construction contract extending the completion date was ever executed by the parties nor were the reasons for the delay and the possible remedies if any accruing to the owner (NEL) discussed by the Board of Directors of NEL.**

APPROVALS (C.C.)

Article 1.1 (b) of the Construction Contract defines approvals as:

> All consents, licenses, authorizations, permits, approvals and certificates required from Regulatory Authorities in respect of the subject matter in question and as at the time in question.

C.D. 001, p. 076

Article 2.1 (b) of the Construction Contract provides that:

> the Owner shall, at its cost and not later than the Commencement Date:
>
> (i) ensure that the Lands are available for commencement of the work;
>
> (ii) ensure that all requisite approvals have been obtained for the commencement of the work and for the location and subsequent operation of the Production Facility on the Lands.

C.D. 001, p. 080

Article 2.6 (a) of the Construction Contract provides:

> The Contractor shall, in the performance of the work and at the Contractor's cost:
>
> (a) ensure that performance of the work is in compliance with all Applicable Laws (subject to the Owner's obligations in this agreement) and shall at its cost obtain all approvals necessary in connection therewith.

C.D. 001, p. 082

Article 2.10 of the Construction Contract provides that:

> Subject to the provisions hereof, the Contractor shall at its cost and expense obtain and maintain in full force and effect, for so long as may be required under Applicable Laws, all approvals from time to time required in respect of the work or any part thereof.

C.D. 001, p. 084

It is noted that the application to construct the Hydroponic Greenhouse Facility was approved at a meeting of the St. John's Metropolitan Area Board on July 2, 1987.

A Development Permit issued July 3, 1987 and valid for one year was forwarded to the contractor subject to numerous conditions, one of which was that an Occupancy Permit was to be obtained from the Board prior to occupancy of the Facility.

C.D. 005, pp. 001-004

No occupancy permit was issued by the St. John's Metropolitan Area Board for the occupancy of the Facility.

C.D. 005, p. 005

On June 20, 1988 the St. John's Metropolitan Area board advised the contractor that matters (deficiencies) remained outstanding with respect to the completion of the Facility in accordance with the conditions of the Development Permit issued July 3, 1987.

C.D. 005, pp. 006-007

It is to be noted one of the conditions of the Development permit was that the Contractor pay an assessment of $84,949.20 relating to the Waterford Valley Relief Trunk Sewer. This assessment was due upon issuance of the building permit. While discussions were held by government, the contractor and Metro Board the matter was never resolved and the assessment to date remains outstanding.

C.D. 005, pp. 008-010

Findings:

- **that the majority of the outstanding matters/deficiencies with respect to completion of the Facility in accordance with the conditions of the Development permit issued to the contractor July 3, 1987 were never resolved /and or rectified.**

- **that the Facility was occupied without the issuance of an occupancy permit by the St. John's Metropolitan Area Board in a breach of Section 207 (d) of the Municipalities Act S.N. 1979 C. 33 as amended.**

- **that while confusion and ambiguity appear to exist as to the responsibility for the obtaining of the occupancy permit pursuant to the provisions relating to approvals aforesaid, the ultimate responsibility appears to be that of the Contractor and Government was remiss in not ensuring that the permit for occupancy was issued prior to NEL's take over and occupancy of the Facility.**

OWNER'S REPRESENTATIVE

Article 2.5 of the Construction Contract provided for the appointment of an Owner's (NEL) Representative. The owner's representative was a civil engineer with the Department of Transportation. His responsibilities were:

1). To inspect, on behalf of Newfoundland Enviroponics Limited, approved plans and designs for those elements of the work for which payments were being made;

2). To meet on a bi-weekly basis with Sprung's project managers to evaluate the status of the work;

3). To review with Sprung's project managers their progress certificates, which would be supplied in writing to him; and

4). To advise the Board of Directors of Newfoundland Enviroponics Limited, in writing as to his opinion on the progress certificates provided by Sprung's Project Managers.

C.D. 001, p. 081
C.D. 005, pp. 011-012

The certificate procedure was to involve a bi-weekly meeting between the Owner's Representative and Sprung's Project Managers, at which meetings Sprung's Project Managers would present a progress certificate indicating the percentage of completion attained to date on each of the items listed in Appendix I (relating to Phase I) and appendix II (relating to Phase II).

C.D. 005, pp. 018-019

APPENDIX I FOR PHASE I

NEWFOUNDLAND ENVIROPONICS LIMITED
ESTIMATED PROGRESS PAYMENT SCHEDULE
CONSTRUCTION CONTRACT PHASE I

Description	Completion	Payment	Completion	Payment	Total
Site Clearing	-	-	-	-	$132,000
Grading	-	-	-	-	$491,700
Fencing	-	-	-	-	$ 79,200
Primary Water Service	-	-	-	-	$142,500
Building Permit	-	-	-	-	$106,900
Civil Works	-	-	-	-	$1,647,700
TOTAL					**$2,600,000**

APPENDIX II FOR PHASE II

SCHEDULE OF WORKS
PHASE II

Monitored	Equipment Value	Labour	Contract Work (Holdback)	Total
Structure Erection	$ —	$281,700	$ —	$281,700
Electrical	481,600	—	237,200	718,800
Plumbing	460,200	—	196,400	656,600
SESE Interior Works	523,100	437,500	—	960,600
Heating System	754,800	—	462,500	1,217,300
Environmental System	106,500	—	29,200	135,700
Interior Infrastructure	—	—	414,500	414,500
Engineering	—	345,200	—	345,200
Commissioning	—	243,000	—	243,000
Production Staff/ Initiating and Transferring	—	135,700	—	135,700
TOTAL				**$5,109,100**

SCHEDULE OF WORKS
OVERHEAD RELATED EXPENDITURES

SIS Erection Equipment and Tool Purchase	498,300
Contractors Facilities	74,000
Sprung Management and Support	495,600
Administration Systems	148,000
	$1,215,900

C.D. 005, pp. 013-015

The items listed and the amounts assigned to each item in Appendix I and Appendix II as well as the Schedule of Works for overhead Related Expenditures were agreed to by Sprung and Government as part of the Construction Contract as per Article 4.2 (ii), (iv) therein. C.D. 001, pp. 085-086

The Owner's Representative was to advise the Board of Directors of NEL as to the acceptability and validity of the progress certificate supplied by Sprung's Project Managers. Based upon the Owners Representative's report, NEL would issue a cheque in the appropriate amount taking into account the requirements of Article 4.3 of the Construction Contract regarding Lien Holdbacks and the requirements of Article 4.8 of the Shareholders Agreement relating to Sprung's shareholders loan (on each progress payment relating to Phase II, one-half of the payment would be advanced to Newfoundland Enviroponics Limited for Sprungs loan equity until the total payments under Article 4.8 Shareholders Agreement reached $3,500,000).

For purposes of the overhead related expenditures, progress payments would be a prorated portion of the Overheads in relation to the proportion of the total payments made under Phase I and Phase II. C.D. 005, pp. 018-019

It is to be noted that the Owner's Representative would not be certifying the quality of work performed nor would the Owner's Representative be guaranteeing to Newfoundland Enviroponics Limited that the Facility would operate or function in any specific manner nor would the Owners Representative be certifying in any manner the suitability of the Facility for agriculture purposes. C.D. 005, pp. 011-012

It is to be noted the Owner's Representative had the necessary expertise in certifying percentages of completion with regard to Phase I. C.D. 005, p. 022

It is noted that both Sprung's Project Manager and the owners representative both indicated they had no expertise in assessing completion percentages with regard to:

Environmental Computer - Hardware
Environmental Computer - Installation
Production Staff - Initiation and Transfer

As a result of Sprung's Project Manager and the Owner's Representatives inability to assess and/or confirm completion percentages in the above noted areas, the manager of Debt Administration with the Department of Finance was instructed to assess completion percentages in those areas.

This official had no expertise in computers and based his assessment of completion on what was told to him by one of the contractor's Senior Management personnel. He could not of his own knowledge confirm if the Facility had the agreed computerization or if what computerization existed was fully operational.

The heretofore official had no knowledge as to what was required with regard to the Production, Initiation and Transfer of plants, and the percentages of completion which were provided to him by one of the Senior Management Personnel of the contractor.

C.D. 005, p. 043
C.D. 005, pp. 023-024
C.D. 005, pp. 181-183

Finding:

- **that the Owner's Representative should have had the necessary expertise to not only certify the percentages of completion but to certify the quality of the work performed and/or the Equipment installed to ensure value was received for payment given and government was remiss in its failure to have such a qualified representative.**

SUBSTANTIAL COMPLETION

It is noted on April 7, 1988 an official of the contractor advised the Board of Directors of Newfoundland Enviroponics Limited that the contractor believed the construction contract was substantially complete, effective April 06, 1988. C.D. 005, p. 046

At a Board of Directors meeting of Newfoundland Enviroponics Limited held on April 28, 1988 substantial completion of the construction contract was accepted, subject to the deficiencies listed as of April 27, 1988 and that holdback funds were to be released upon expiration of the Mechanics Lien Period. C.D. 005, pp. 047-059

It is noted the balance in the Holdback account as of May 5, 1988 was $1,410,420 and of that sum the amount of $585,420 was forwarded to the contractor, the balance of $825,000 was held in the Holdback Account accruing interest until November 16, 1988 (the $825,000 was security for the governments guarantee to the Contractor for $825,000 authorized December 17, 1987). C.D. 005, p. 061

On November 16, 1988 the sum of $803,320 was paid to the contractor who in turn paid the Royal Bank $778,449.04 on November 18, 1988.

$75,000 was subsequently paid from the Holdback Account to Tors Cove Excavating Company Limited (as referenced under the Heading Governments Involvement in the Legal Process) and the balance, in interest was paid to the contractor in January of 1989. C.D. 010, pp. 085-088 C.D. 011, pp. 022-025

The deficiencies as of April 27, 1988 amounted to $78,500. On May 5, 1988 there was no confirmation that the aforesaid deficiencies were rectified nor was a holdback maintained for such deficiencies. C.D. 005, p. 060

It is noted Sprung's Project Managers advised the owners representative in writing on October 20, 1988 that:

> "the Facility is now substantially functional for its intended purpose. All zones including the pre production one are either in operation or ready to operate". Sprung's Project Manager further advised

> "the absence of detailed drawings and specifications, the absence of criteria of acceptance for a used prototype Facility and the need to inspect the Facility for deficiencies, all combine to limit our ability to state that the project is substantially complete other than from the point of view of its intended purpose."

C.D. 005, pp. 062-065

Findings:

- **that Substantial Completion of the Facility on April 6, 1988 was not confirmed by the Owner's Representative nor even by Sprung's Project Manager as it was on October 20, 1988 with the limitations therein noted.**

- **that Sprung's Project Manager as well as the Owner's Representative did not have the expertise "to inspect the Facility for deficiencies as they themselves advised".**

- **that the proper expertise should have been provided certainly on behalf of the owner, Newfoundland Enviroponics Limited to ensure the Facility was not deficient and to ensure that monies were not paid while deficiencies were outstanding.**

PART X

ENVIRONMENTAL ASSESSMENT

Section 2 (e) (iii) of the Environmental Assessment Act defines "environment" as:

> "the social, economic, recreational cultural and aesthetic condition and factors that influence the life of humans or a community".

Section 2 (f) defines "environmental assessment" as:

> "a process by which the environmental impact of an undertaking is predicted and evaluated before the undertaking has begun or occurred".

Section 2 (N) defines "undertaking" as:

> "any enterprise, activity, project, structure, work, policy, proposal, plan or program that may in the opinion of the Minister, have a significant environmental impact and includes a modification, an extension an abandonment, a demolition and a rehabilitation thereof".

The policy of the Department as it then existed in interpreting the term "undertaking" was that a project or proposal automatically becomes an "undertaking" if it fitted the categories, conditions, defined in schedules 1 and 2 of the regulations. These schedules provide for significant environment impact as defined. Beyond that, unless the project proposal was exempted under the legislation, the Department interpreted the Environment Assessment Act to allow the Minister to define anything, as an "undertaking" contingent, on the Minister deciding that "it may have a significant environmental impact".

C.D. 005, pp. 068-121

It is to be noted in June of 1987 officials of the Department of Environment met with Mr. Philip Sprung and an official of the Premier's Office, where the proposal for the Hydroponic Greenhouse was outlined verbally. Based on the project description as presented, which included no reference to artificial lighting, officials advised, the project was not registrable and therefore could proceed.

C.D. 005, p. 122

By (M/C 138-89) dated February 10, 1989 a special warrant in the amount of $64,910 was issued in favour of the Department of RAND to accommodate grants to Pointsetta Growers in the vicinity of the Sprung Greenhouse, to assist with losses in the 1988 year and with respect to future operations. C.D. 005, p. 123

By Section 6 (1) of the Environmental Assessment Act every proponent shall:

> "before proceeding with the formal design of an undertaking, notify the Minister in writing on a prescribed form concerning the proposed undertaking".

By Section 6 (2) the notification under subsection (1) is:

> "deemed to be registration of an undertaking for the purposes of the Act".

Findings:

- **that at the time of the meeting with officials of the Department of Environment it was a fact that growing lights would be an integral part of the proposal and should have been mentioned as such by those of Government who were involved in negotiations with Sprung. Once mentioned it would have been for officials of the Department of Environment to determine whether an environmental impact study was warranted to determine the effect, if any, on the near by community.**

- **that the payment of $64,910 to the Poinsettia Growers in the vicinity of the Sprung Greenhouse to assist with losses in the years 1988 clearly indicated there existed an impact to the Environment by virtue of the said Greenhouse.**

- **that the Minister was not notified in writing of the design of the Hydroponic Facility as he should have been pursuant to the existing legislation.**

INVOLVEMENT OF GOVERNMENT IN THE LEGAL PROCESS

On May 13 1988 Tors Cove Excavating Limited registered a Mechanics Lien against SESE (the contractor) and NEL (the owner) for $106,441.59. The Lien was for Excavation services supplied on the site at the request of the contractor.

On May 27 1988 Tors Cove Excavating Limited issued a Statement of Claim against SESE and NEL for $106,441.59. C.D. 005, pp. 171-174

By correspondence dated July 9, 1988 a Government appointed Director of NEL advised the Deputy Minister of RAND of actions against SESE, including the action initiated by Tors Cove Excavating Limited and indicated that Philip Sprung and his counsel were of the view that a sound legal position existed in defence of the action by Tors Cove Excavating Limited. The Government appointed Director indicated that both he and another director of NEL felt government should not involve itself in the matter and that the action should follow the normal legal procedure. C.D. 005, pp. 175-176

By Cabinet Directive dated July 13 1988 it was directed amongst other things that:

> "the Government Directors of NEL seek to ensure that Lubys Excavating Mechanics Lien be retired". (Luby refers to one of the principals of Tors Cove Excavating Limited). C.D. 005, p. 042

By Cabinet Directive dated November 17, 1988 it was directed that:

> "Government representatives on the Board of Directors of NEL support a fund settlement of $75,000 with Luby Excavating Limited". C.D. 005, pp. 179-180

By correspondence dated December 8, 1988 a Government appointed Director of NEL forwarded to Counsel for NEL the sum of $75,000 from the holdback account to settle the Tors Cove Excavating Limited Claim. The claim of Tors Cove Excavating Limited was with all reasonable certainty settled for the sum of 75,000. C.D. 005, pp. 179-180

C.D. 005, pp. 175-176
C.D. 005, pp. 184-185

It is to be noted other actions were initiated against SESE and NEL and were determined through the normal legal process without intervention by Government.

Finding:

. that the direct involvement of government in settlement of the Tors Cove Excavating Limited's claim was inappropriate, unwarranted and smacked of favouritism.

PART XI

TERMS OF REFERENCE

The previous eight parts of the report deal with the involvement of Government into specific areas related to and associated with the joint venture undertaking and encompasses Governments initial assessment, commitment, expenditure and determination of the operation of the joint venture upon the appointment of a Receiver Manager on March 3, 1989. Specific findings have been made in relation to matters which bear directly on Governments involvement with the noted companies. In determining and responding therefore to the specific Terms of Reference set forth in paragraph I of the Commission (Terms of Reference), a brief response will then suffice.

The Commission document dated July 1st, 1990, sets forth the Terms of Reference as therein noted.

Generally, the Terms of Reference provide for an Enquiry Into the Involvement of the Government of Newfoundland and Labrador and any of its Agencies or Corporations with Sprung Sales Limited, Sprung Environmental Space Enclosures Limited or Newfoundland Enviroponics Limited. To determine the relevant time frame for such an enquiry, it must be determined when in fact Government involvement commenced and when in fact Government involvement ceased.

Findings:

- **that Government's involvement with the noted Sprung Companies and in particular Sprung Environmental Space Enclosures Limited can realistically be said to have commenced in early 1987 while Government's involvement with Newfoundland Enviroponics Limited the Joint Venture Company can be said to have commenced on or about June 25, 1987 upon Execution of the Legal Agreements.**

- that Government's direct involvement with Newfoundland Enviroponics Limited can be said to have ceased for all intents and purposes upon the appropriate amendments to the Loan and Guarantee Act 1957 being brought before the House of Assembly on June 30, 1989 for ratification.

The Specific Terms of Reference:

1.(a) whether the expenditure of and accounting for government financial and other assistance was in all respects proper, properly managed and accounted for;

Findings:

- that the Government commitment to the purchase and erection of the hydroponics Facility for a contract price of $14,325,000 was improper in that adequate proper and due investigation of the technology and economic viability of the proposal was not carried out prior to Government's commitment to the Project. It appears that the contract price of $14,325,000 for the hydroponics Facility was excessive for what the Company received.

- that the Project was a relatively large one with considerable financial risk and commitment of public funds. Hydroponics technology for growing crops on a mass production basis was being introduced to Newfoundland. Notwithstanding the $35,000,000 in research and development alleged to have been spent by Sprung on the hydroponics process, there was indeed uncertainty about the economic viability of this rather large venture with markets for its products yet to be developed and unproven production methodology. The need for timely and effective financial and management reporting and accounting information was paramount for managing and controlling a project where public funds were being committed. Sprung, one of the joint owners, had a significant influence over the operation and development of the Facility. Safeguards were not built into the approval process to ensure that, under circumstances of significant influence, costs were being paid at no more than competitive prices. Business plans, operating budgets, cash forecasts, monthly detailed financial statements and analysis prepared in accordance with generally accepted accounting standards and practices were inadequate for a project with such a high degree of risk and commitment of public funds.

- that lack of proper management and accounting information made it impossible to determine whether all revenue and expenditures of the Project were properly accounted for and whether the transactions were proper in all other respects. The accounting for the Project prepared by Commission Accountants presented the financial operations of the entity on a cash basis. The review of the accounting transactions revealed that provisions of the Shareholders Agreement and the Construction Agreement were not always adhered to. Major changes to the Agreements were in fact noted but only one was reduced to writing as a formal amendment to the Construction Agreement.

- that the Province invested some $22,208,021 in the Project whereas Sprung invested only $4,000,000. NEL was a joint venture between the two parties. At the outset the Province and Sprung were prepared to invest $3,500,000 each as joint owners with the Province and Sprung guaranteeing bank loans for capital expenditures by NEL to the extent of $7,000,000 and $500,000 respectively. Working capital financing and debt financing for the growing lights were to be the responsibility of NEL itself. It can be said, therefore, that the Province's excess funding over its initial commitment was an improper expenditure of public funds. The excess funding by the Province was not invested according to the Agreements entered into between the two joint owners.

- that deficiencies in construction, although relatively small, were apparently never completed although holdbacks (with interest) were released in entirety to the Contractor, Sprung. Over 61% of the disbursements by NEL for capital assets and operating expenditures were to Sprung and related parties, entities which had significant influence over NEL as to what it paid for its purchases and how it operated. Financial provisions in the Agreements for such items as energy, retail sales taxes, investment tax credits, turnkey operations to name a few, were not properly adhered to nor were the Agreements formally amended.

- that the expenditure by Government of $13,925,000 pursuant to loan guarantees was improper in that Government clearly ignored the established guidelines/conditions for the granting of loan guarantees for such a project.

- that Government failed to account for loan guarantees by failing to heed the convention of bringing the various loan guarantees before the House of Assembly and therefore acted in an improper fashion and indeed breached the covenant to the Royal Bank of Canada set forth in the various noted guarantees by failing to bring the said guarantees before the House of Assembly for ratification as an amendment to the Loan and Guarantee Act thereby ensuring their legal enforceability.

(b) whether any Acts and Regulations of the Province of Newfoundland were not complied with;

Findings:

- **that the Retail Sales Tax Act S.N. 1978 C. 36 as amended and in particular Section 6 was not complied with in that no tax was paid on the fair value of the tangible personal property used in the construction of the Facility; that Section 48 was not complied with in that no sum was deposited or bond furnished as therein required.**

- **that the intent of The Loan and Guarantee Act 1957 was not complied with in that the various loan guarantees by Government on behalf of Newfoundland Enviroponics Limited as heretofore noted were not brought before the House of Assembly as the legislation intended and as convention dictated.**

- **that the Municipalities Act S.N. 1979 C. 33 as amended and in particular Section 207 (d) thereof was not compiled with in that the Hydroponic Facility was occupied without the issuance of an occupancy permit by the St. John's Metropolitan Area Board.**

- **that the Environmental Assessment Act S.N. 1980 C. 3 as amended was not compiled with in that the Minister of the Environment was not notified in writing of the proposed project as he should have been.**

(c) whether or not there were breaches of any of the arrangements or agreements between the Government of Newfoundland and Labrador and any of the companies;

(1). Findings with regard to breaches of the Shareholders Agreement:

- that there was no refund of tax paid under the Retail Sale Tax Act pursuant to Article 4.3 (b) and no issuance of Class "C" Shares equal to the value of the said refund as determined by auditors designated by Government following completion of construction of the Facility pursuant to Article 4.5 (b).

- that the guarantees referred to in paragraphs 4.3 (a) and 4.4 (c) and the related security documentation was not provided in accordance with Article 4.7 nor was a later date agreed to by the parties in writing.

- that Government did not consent pursuant to Article 7.1 (ii) to benefits of rent, air fare and relocation costs for management employees of Newfoundland Enviroponics Limited nor were such benefits approved by the Board of Directors of Newfoundland Enviroponics Limited.

- that Newfoundland Enviroponics Limited did not pay to Government the sum of $25,000 for engineering services respecting the land pursuant to Article 7.4.

- that Newfoundland Enviroponics Limited did not maintain records of operation at the Facility pursuant to Article 9.5 to enable energy calculations to made as required by Article 9.3.

- that no meters were installed at the Facility to permit the measurement of electricity consumed in operation of the growing lights separate from the measurement of other electricity consumed at the Facility, pursuant to Article 10.4.

- that the change to the Shareholders Agreement pertaining to the Lease for Lights purchase pursuant to Article 10.1 in relation to electrical charge backs by the Sprung noted companies as contractor to Newfoundland Enviroponics Limited as owner was not in accordance with Article 7.1 (ix) which required the consent of Government for "any transactions between the Company and Sprung other than those specifically permitted by the Shareholders Agreement".

(2). The generality of the Terms of Reference permit comment on the Construction Agreement.

Findings with regard to breaches of the Construction Agreement:

- that payment of $4,000,000 pursuant to Article 4.2 (iii) was not in accordance with the provision as therein set forth nor was the payment made in accordance with Article 4.2 (iii) as amended.

- that interest of $88,900 accruing in the Mechanics Lien holdback account should not have been paid by Newfoundland Enviroponics Limited as owner to or for the benefit of one of the Sprung noted companies as contractor.

- that the completion date of construction was not in accordance with Article 1.1 (f) (180 days from the execution of the Construction Agreement on June 25, 1987) and no amendment to the Construction Agreement was executed extending the completion date although the contractor did in fact request a ninety day extension.

- that no occupancy permit was obtained from the St. John's Metropolitan Area Board permitting occupancy of the Facility or part there of as required by Articles 2.6 and 2.10.

- that a major change to the Construction Agreement in that initiation and transfer would take place as soon as each production zone came on stream and that the Sprung noted companies as contractor would be reimbursed its costs of maintaining each crop by Newfoundland Enviroponics Limited the owner subsequent to each initiation until all eight production zones were initiated or planted, did not have the necessary consent of Government as required by Article 7.1 (ix) of the Shareholders Agreement.

(d) whether there was any other aspect of Governmental involvement in the matter that had a significant adverse impact on the interests of the Province and should be brought to the attention of the Lieutenant-Governor in Council;

Findings:

- that Government did not have the required and independent Expertise to properly evaluate the Sprung proposal nor did Government seek the required Expertise. Government, when once committed to the joint venture, failed to obtain the necessary Expertise to advise Government on the progress or otherwise of the venture and continued to commit and sustain direct financial loss without the proper and necessary consultation. Government relied entirely for whatever reason on what was put forth by the proponent of the proposal to its detriment.

- that the Financial risk of the project was almost entirely with Government without justification, in spite of the fact that Newfoundland Enviroponics Limited was a joint venture operation between Government and the Sprung noted companies.

2.AND FURTHER, We require you, the Commissioner, to bring forward conclusions and recommendations with respect to measures which may be taken by the Government of Newfoundland and Labrador to prevent any future developments being undertaken without appropriate safeguards.

I make the following recommendations without the benefit of public hearings:

- The viability of future developments with Government financial participation should be assessed by independent consultants with the necessary expertise, to ensure that Government financial participation is warranted and acceptable not only from a business perspective but also from the appropriate political perspective and that Government has the necessary security for its financial participation as is warranted.

- Government should not participate in joint venture companies through Shareholdings and as members of the Board of Directors. Governments are elected to govern and impliedly do not have the required expertise to participate in developments and projects, the operation, management and ownership of which are best left to those who have the required expertise and the appropriate capital.

- Governments proposed financial commitment to developments should be fully debated in the House of Assembly prior to Governments actual commitment of public funds to such developments and any subsequent Government financial commitment arising should be fully debated in the House of Assembly prior to expenditure of same. Should the House of Assembly not be sitting and Expenditure is required on an urgent basis, debate on same should commence at the earliest opportunity in the Next Session.

- Government should have access to a systematic flow of timely, pertinent information to allow it to judge whether Government financial participation in developments, where significant financial exposure of public funds exists, have met their stated objectives for each fiscal period. Such entities should be required to report at least annually:

    a). their objectives, strategies and expected performance;

    b). the extent to which objectives have been achieved with explanations for significant variances between planned and actual performance;

    c). quantitative performance information as considered appropriate.

GLOSSARY

ASM	Air-tite Sheet Metal
APEN	Association of Professional Engineers of Newfoundland
AGD	The Department of the Auditor General
AEP	Atlantic Employment Program
BFS	Basic Financial System
Board	Board of Directors of NEL
CD	Cabinet Directive
Company	(NEL) Newfoundland Enviroponics Limited
C.A.	Construction Agreement
Contractor	Sprung Environmental Space Enclosures Limited/Sprung Instant Structures Limited
DEL	Delta Electric Limited
DOD	Department of Development
DOF	Department of Finance
DOJ	Department of Justice
DRIE	Department of Regional Industrial Expansion
E&L	Department of Environment and Lands
E&Y	Ernst and Young
EC	Executive Council
FST	Federal Sales Tax
Government	Her Majesty the Queen in Right of Newfoundland
Heads of Agreement	Agreement in Principle
Hydroponics	A system of growing fruits and vegetables without the use of soil

Initiation Planting

I.T.C. Investment Tax Credit

K.V.A. Kilovoltampere

K.W.H. Kilowatt Hours

Langleys Unit of Light Measurement

Lights Growing Lights

MC Minutes of Council

NIDC Newfoundland Industrial Development Corporation

NLP Newfoundland Light and Power Limited

NEL Newfoundland Enviroponics Limited

N.E.L. New-Land Enterprises Limited

NKHK Noseworthy Keating Howard Kung

OC Order in Council

Owner Newfoundland Enviroponics Limited

P.P.Z. Pre-production Zone

PEI Prince Enterprises Limited

P.Z. Production Zone

Province Government of Newfoundland and Labrador

R.A.N.D. Department of Rural, Agricultural and Northern Development

RST Retail Sales Tax

RBC Royal Bank of Canada

RCMP Royal Canadian Mounted Police

RNC Royal Newfoundland Constabulary

SMB St. John's Metro Board

STA School Tax Authority

S.A. Shareholders Agreement

SHL Snellen Holdings Limited

SESE Sprung Environmental Space Enclosures Limited

SFD Sprung Floppy Disks

SHD Sprung Hard Disks

SIS Sprung Instant Structures Limited

S.S.L. Sprung Sales Limited

Sylvania GTE Sylvania Canada Limited

T.T.A. Technology Transfer Agreement

TML Tekcon Management Limited

Transfer Pre-production zone to production zone

UFCW United Food and Commercial Workers

WST Department of Works, Services and Transportation

WCC Workers Compensation Commission

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